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Calendar No. 41

98TH CONGRESS 1st Session } SENATE { REPORT No. 98-23

SOCIAL SECURITY ACT AMENDMENTS OF 1983

MARCH 11 (legislative day, MARCH 7), 1983.—Ordered to be printed

Mr. DOLE, from the Committee on Finance, submitted the following

REPORT

[To accompany S. 1]

The Committee on Finance to which was referred the bill (S. 1) to implement the consensus recommendations of the National Commission on Social Security Reform, having considered the same, reports favorably thereon with an amendment and recommend that the bill do pass.

SOCIAL SECURITY (OASDI) PROVISIONS

ACTUARIAL ANALYSIS

The OASDI estimates in the following sectional descriptions were prepared by the office of the Actuary, SSA and are based on 1983 Trustees II-B assumptions. Under those assumptions, the Committee amendments described below would permit the timely payment of social security cash benefits through the short-range (1983–89). In the long-range, the Committee amendments are projected to meet or slightly exceed the long-deficit identified by the National Commission on Social Security Reform of 1.80 percent of taxable payroll (revised under 1983 Trustees II–B assumptions to 2.09 percent of taxable payroll).

These amendments are also projected to have a significant impact on the Hospital Insurance (HI) trust fund. CBO estimates project an increase in the HI trust fund of $14.6 billion over the period fiscal years 1983–88.

The amendments also impact on other Federal programs. To the extent the cost/savings are reflected in the following descriptions, they have been provided by CBO and are based on CBO's February 1983 assumptions. A table showing the impact of these amend-

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ments on the total Federal budget deficit is located following the sectional descriptions.

[Memorandum]

DEPARTMENT OF HEALTH AND HUMAN SERVICES,
SOCIAL SECURITY ADMINISTRATION,
March 11, 1983.

To: Mr. Harry C. Ballantyne, Chief Actuary.
From: Francisco R. Bayo, Deputy Chief Actuary.
Subject: Preliminary estimate of the impact of S. 1, as reported by the Senate Finance Committee on the long-range financial status of the OASDI system.

The attached table includes preliminary long-range estimates for S. 1. as reported by the Senate Finance Committee based on the 1983 Trustees Report Alternative II-B assumptions. Enactment of this bill will result in a long-range actuarial surplus of 0.08 percent of taxable payroll for OASDI combined. Estimates for individual provisions are shown in the table generally only for those provisions with significant long-range impact on OASDI. However, the impact on OASDI of all provisions of S. 1. as reported is included in the totals.

The estimates assume that the allocation to the DI trust fund will be similar to the allocation in H.R. 1900 as reported by the Ways and Means Committee, except that after 1999 the rate would increase from 0.60 to 0.65 each.

FRANCISCO R. BAYO,
Deputy Chief Actuary.

Attachment.

TABLE 1.—ESTIMATED CHANGES IN OASDI TAX INCOME OR BENEFIT OUTGO UNDER S. 1 AS REPORTED BY THE SENATE FINANCE COMMITTEE, BASED ON 1983 ALTERNATIVE II–B ASSUMPTIONS

[In billions of dollars]

Provision	Calendar year—							
	1983	1984	1985	1986	1987	1988	1989	Total, 1983–89
Increase tax rate on covered wages and salaries		8.6	0.3			14.5	16.0	39.4
Increase tax rate on covered self-employment earnings		1.1	3.1	3.0	3.2	3.7	4.4	18.5
Cover President, Vice-President, and Members of Congress		(1)	(1)	(1)	(1)	(1)	(1)	(1)
Cover new Federal employees		.2	.7	1.2	1.8	2.4	3.1	9.3
Cover all nonprofit employees		1.3	1.5	1.8	2.1	2.6	3.1	12.5
Total for new coverage		1.5	2.2	3.0	3.9	5.0	6.1	21.8
Prohibit State and local government terminations		.1	.2	.4	.6	.8	1.1	3.2
Accelerate collection of State and local taxes		1.4	.1	.1	.1	.3	.2	2.2
Provide general fund transfers for military service credits and unnegotiated checks	19.2	−.4	−.4	−.3	−.3	−.3	−.3	17.2
Delay benefit increases 6 months	3.2	5.2	5.4	5.5	6.2	6.7	7.3	39.4
Tax ½ of benefits for high income beneficiaries		2.6	3.2	3.9	4.7	5.6	6.7	26.6
Continue benefits on remarriage		(2)	(2)	(2)	(2)	(2)	(2)	−.1
Modify indexing of deferred survivors' benefits		(2)	(2)	(2)	(2)	(2)	(2)	(2)
Raise disabled widow(er)'s benefits to 71.5 percent of PIA		−.2	−.2	−.2	−.2	−.3	−.3	−1.4
Pay divorced spouses whether or not worker has retired		(2)	(2)	(2)	(2)	(2)	(2)	−.1
Replace 90-percent factor in benefit formula with variable percentage, for individuals receiving pensions from covered employment		(3)	(3)	(3)	(3)	.1	.1	.3
Raise delayed retirement credit, beginning in 1990								

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TABLE 1.—ESTIMATED CHANGES IN OASDI TAX INCOME OR BENEFIT OUTGO UNDER S. 1 AS REPORTED BY THE SENATE FINANCE COMMITTEE, BASED ON 1983 ALTERNATIVE II-B ASSUMPTIONS—Continued

[In billions of dollars]

Provision	Calendar year—							
	1983	1984	1985	1986	1987	1988	1989	Total, 1983–89
Provide up to 2 child-care drop out years		(2)	−.1	−.1	−.2	−.4	−.5	−1.3
All other miscellaneous and technical changes		(2)	(2)	(2)	(2)	(2)	(2)	−.1
Total for all changes	22.3	19.9	13.8	15.1	17.9	35.6	40.8	165.5

[1] Net additional taxes of less than $50 million.
[2] Additional benefits of less than $50 million.
[3] Reduction in benefits of less than $50 million.

Note: Estimates shown for each provision include the effects of interaction with all preceding provisions. Totals do not always equal the sum of components due to rounding. Positive figures represent additional income or reductions in benefits. Negative figures represent reductions in income or increases in benefits.

Source: Social Security Administration, Office of the Actuary, March 11, 1983.

PRELIMINARY ESTIMATED LONG-RANGE OASDI COST EFFECT OF S. 1 AS REPORTED BY THE SENATE FINANCE COMMITTEE

Provision	Effect as percent of payroll		
	OASI	DI	OASDI
Present law:			
Average cost rate	13.04	1.34	14.38
Average tax rate	10.13	2.17	12.29
Actuarial balance	−2.92	+.83	−2.09
Changes relating to both long-range and short-range financing: [1]			
Cover new Federal employees	+.26	+.02	+.28
Cover all nonprofit employees	+.09	+.01	+.10
Prohibit State and local termination	+.06	+.00	+.06
Delay benefit increases 6 months	+.28	+.03	+.30
Stabilize trust fund ratio			
Eliminate "windfall" benefits	+.05	+.00	+.05
Raise delayed retirement credits	−.10		−.10
Tax ½ of benefits	+.57	+.05	+.62
Accelerate tax rate increase	+.03		+.03
Increase tax rate on self-employment	+.17	+.02	+.19
Change DI rate allocation	+.90	−.90	
Continue benefits on remarriage	−.00	−.00	−.00
Pay divorced spouse of nonretired	−.01	−.00	−.01
Modify indexing of survivor's benefits	−.05		−.05
Raise disabled widow's benefits	−.01		−.01
Modify military credits financing	+.01	+.00	+.01
Credit unnegotiated checks	+.00	+.00	+.00
Tax certain salary reduction plans	+.03	+.00	+.03
Limit benefits to nonresident aliens	+.01	+.00	+.01
Eliminate benefits to incarcerated felons	+.00	+.00	+.00
Subtotal for the effect of the above provisions [2]	+2.22	−.78	+1.44
Remaining deficit after the above provisions	−.70	+.05	−.65
Additional changes relating primarily to long-range financing: [3]			
Modify benefit formula after this century	+.39	+.04	+.43
Raise normal retirement age to 66	+.48	−.08	−.40
Eliminate earnings test at age 65	−.05		−.05
Add up to 2 child care dropout years	−.03	−.00	−.04
Total effect of all of the provisions [4]	+2.99	−.82	+2.17

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PRELIMINARY ESTIMATED LONG-RANGE OASDI COST EFFECT OF S. 1 AS REPORTED BY THE SENATE FINANCE COMMITTEE—Continued

Provision	Effect as percent of payroll		
	OASI	DI	OASDI
After committee bill:			
Actuarial balance	+.07	+.01	+0.8
Average income	11.61	1.31	12.92
Average cost rate	11.54	1.30	12.84

[1] The values for each of these individual provisions represent the effect over present law and do not take into account interaction with other provisions.
[2] The values in the subtotal take into account the estimate interactions among the provisions.
[3] The values for each of these provisions take into account interaction with the provisions included in the subtotal.
[4] The values for the total effect of S. 1 take into account interactions among all of the provisions of the bill.

Note: The above estimates are based on the 1983 Trustees Report Alternative II–B assumptions. Individual estimates may not add to totals due to rounding and/or interaction among proposals.

Source: Office of the Actuary, March 11, 1983.

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Summary of Social Security (OASDI) Provisions

Coverage of newly hired Federal employees

Extend social security coverage to all Federal civilian employees hired after 1983 (unless their break in Federal service has been for one year less), and to all current members of Congress, the President, Vice President, the Social Security Commissioner, and to current Congressional staff not already covered under a Federal staff retirement system, as of January 1, 1984. Also, states that "Nothing in this Act shall reduce the accrued entitlements to future benefits under the Federal retirement system of current and retired Federal employees and their families."

Coverage of nonprofit employees

Extend social security coverage on a mandatory basis to all employees of nonprofit organizations, effective January 1, 1984.

Prohibit withdrawl of State and local employees

Prohibit State and local governments from terminating coverage for their employees. Pending terminations would be invalid, effective on enactment. In addition, provide an opportunity for State and local governments which have withdrawn from the social security system to voluntarily rejoin. Once having rejoined, the governmental entity would be precluded from terminating coverage.

Tax exemption for the Amish

Extend the social security tax exemption now applicable to the self-employed Amish to the Amish who are employees of the Amish.

Delay cost-of-living adjustment to a calendar year basis

Provide the automatic cost-of-living adjustment of social security benefits on a calendar year basis. Beginning in 1983, the COLA for OASDI benefits would be applied to the December benefit, which is payable at the beginning of January. For 1983, the COLA would be calculated as under current law (i.e., the change in the CPI for the third quarter of a year over the CPI for the third quarter of the previous year). This would ensure that the lag between the end of the period over which the COLA is measured and the time the COLA is actually applied to benefits remains 3 months. For 1983 only, the COLA would be given even if it is less than 3 percent. The SMI (Supplemental Medical Insurance) premium increase would also be delayed.

Eliminate "windfall" benefits

Reduce (but not eliminate) social security benefits for retired and disabled workers who first become eligible for a pension based on

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non-covered employment after 1983. For such workers, the heavily weighted 90 percent factor in the benefit formula would be replaced by a factor of 32 percent, phased in over a five year period. Social security benefits would in no case be reduced by more than one-third of the portion of the worker's pension based on service which was non-covered employment. Also, the percentage reduction in the benefit formula would be limited to no more than 10 percentage points for each year coverage falls shorts of 30 years. Survivor benefits would not be affected by this provision.

Benefits for divorced or disabled widows or widowers who remarry

Allow benefits to continue to be paid to certain beneficiaries upon remarriage if that marriage takes place after the age of first eligibility. Benefits would be payable to: disabled widow(er)s and disabled surviving divorced spouses who remarry after age 50, and to surviving divorced spouses who remarry after 60. No change would be made in the current dual entitlement provision of the law which allows only the highest benefit to which an individual is eligible to be drawn.

Changes in indexing for deferred survivor benefits

Provide that deferred widow and widower benefits would continue to be based on earnings indexed to wages as under present law, however, this wage indexing would continue after the death of the worker. Such wage indexing would apply through the year the worker would have reached age 60, or two years before the survivor becomes eligible for aged or disabled widow's (or widower's) benefits, whichever is earlier.

Independent eligibility for divorced spouses

Allow divorced spouses (who have been divorced for a significant period) to draw benefits at age 62 if the former spouse is eligible for retirement benefits, whether or not the former spouse has claimed these benefits or has had them suspended because of substantial employment.

Increase benefits for disabled widows and widowers

Increase benefits for disabled widow(er)s age 50–59 to 71.5 percent of the primary insurance amount, the amount to which widow(er)s are entitled at age 60.

Adjustment of cost-of-living increase when trust fund ratio falls below 20 percent

Modify the cost-of-living adjustment formula during periods when trust fund reserves are low in order to help stabilize reserves. Beginning with 1988, if the OASDI trust fund ratio (reserves as a percentage of outgo) as of the beginning of a year is less than 20 percent, the adjustment of OASDI benefits would be based on the lower of the increase in the CPI or average wages. When the balance in the trust funds has risen to at least 32 percent of estimated annual outlays, "catch-up" payments would be made beginning the following year. This would not apply to the COLA for the Supplemental Security Income (SSI) program.

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Increase delayed retirement credit

Gradually increase, between 1990 and 2010, the delayed retirement credit from 3 percent to 8 percent per year.

Increase social security retirement age

Gradually raise the social security retirement age to 66 by the year 2012, beginning with those who attain age 62 in 2000. Early-retirement benefits would continue to be available at age 62 for workers and spouses and at age 60 for widows and widowers, but the actuarial reduction factors would be larger.

Long-range benefit change

For workers first becoming eligible for benefits in 2000, reduce initial benefit levels by about 5 percent by decreasing the percentage factors in the benefit formula by two-thirds of one percent each year for 8 years.

Elimination of retirement earnings test

Gradually phase out, between 1990 and 1994, the retirement earnings test for people 65 and older. The exempt amount of earnings would be increased by $3,000 in 1990 and in each of the next four years, with the earnings test (for people 65 and older) completely eliminated in 1995.

Child-care dropout years:

Allow two years to be dropped out of the formula for computing social security benefits for persons who leave the workforce to care for children under age 3 at home. Presently, the worker's five lowest years of earnings are dropped in the computation of the worker's earnings history. To qualify for an additional childcare dropout year, a person can not have any earnings during the year.

Prisoners benefits

Eliminate all benefits to felons during their period of incarceration. Benefits of dependents and survivors of incarcerated felons would not be affected.

Limitation on benefits to aliens

In the future, eliminate benefits to alien workers, their dependents and survivors who reside abroad. As a result, no benefits would be paid to alien dependents of alien workers who were acquired (through marriage, birth or adoption) while outside the United States. However, benefits would be paid under the following conditions:

(1) the worker is the citizen of a country with which the United States has a treaty or totalization agreement which provides for reciprocity of social security coverage; and

(2) benefits would continue until total benefits (excluding any withheld taxes) paid to the wage earner and dependents equal taxes paid by the wage earner plus interest.

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Fail-safe

To ensure the timely payment of social security benefits during periods when OASDI trust fund reserves are less than 20 percent of annual outgo and are also projected to decline, the Committee agreed to require the Secretary of Health and Human Services to reduce the COLA to the extent necessary to prevent a decline in reserves. The Secretary will first reduce (or withhold) increases for people with benefits which are based on a primary insurance amount above $250 (monthly amount). If necessary, however, people with benefits at or below that level may also have their increases reduced. At a maximum, there would be no benefit increase for anyone. The Secretary would have to notify Congress by July 1 of each year in which he finds that action to limit the next COLA would be required, thereby giving Congress time to enact an alternative solution to the potential funding problem. The provision would apply only after the use of all other provisions, such as interfund borrowing, which are designed to ensure adequate trust fund balances.

Taxation of social security benefits for higher income persons

Subject social security and tier one railroad retirement benefits to income tax based on thresholds of $25,000 for single taxpayers, $32,000 for married taxpayers filing joint returns, and $0 for married taxpayers filing separate returns. To determine whether the taxpayer's income exceeds these thresholds, one-half of social security benefits and all tax-free income would be added to adjusted gross income and tax-exempt interest. For taxpayers over the threshold, the lesser of one-half of social security benefits or one-half of the excess combined income over the threshold amount would be subject to income tax.

Beginning in 1984 the Secretary of the Treasury would be required to transfer to the appropriate trust funds, on at least a quarterly basis, the revenues estimated (on the basis of tax liability to be generated from this provision for that quarter.

Acceleration of increase in FICA taxes; 1984 employee FICA tax

Revise the OASDI tax schedule so that the 1985 rate would be moved to 1984, the 1985–87 rate would remain as scheduled under present law, part of the 1990 rate would be moved to 1988, and the rate for 1990 and after would remain unchanged. The HI tax rates for all years would remain unchanged. For 1984, a refundable tax credit would be provided in the amount of the increase in the employee taxes over what would have been payable under present law: 0.3 percent of taxable wages.

The 1984 refundable tax credit would be allowed against 1984 employee FICA and Tier One Railroad Retirement taxes rather than against income tax.

Self-employment taxes; tax credit against self-employment tax

Make the self-employed OASDI tax rate equal to the combined employer-employee rate, beginning in 1984, as those rates are rescheduled. In addition, the HI tax for the self-employed would be

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doubled to make it equivalent to the combined employer-employee rate. A credit against self-employment taxes would be provided.

Reallocation of OASDI tax rate

Reallocate the OASDI tax so that both the OASI and the DI trust funds will have about the same reserve ratios (i.e., reserves at the beginning of the year as a percentage of outgo during the year).

Interfund borrowing extension

Authorize, through 1987, interfund borrowing between the OASI, DI and HI trust funds, protections provided for each trust fund.

Credit amounts of unnegotiated checks to the trust funds

Provide for a lump sum payment to the OASDI trust fund from the General Fund representing the amount of uncashed benefit checks which have been issued in the past. In addition, require credit the trust funds on a regular basis with an amount equal to the value of all OASDI benefit checks which have not been negotiated for a period of twelve months.

Military wage credits

Credit the OASDI trust fund, in a lump sum, with an amount equal to the estimated additional cost of providing future benefits based on pre-1957 military wage credits. In addition, the OASDHI trust funds would be credited with a lump sum payment equaling the taxes that would have been collected and the interest that would have been earned if the credits for service after 1956 and before 1983 had been taxed as they were earned, less the reimbursements already received. Beginning in 1983, a general fund appropriation would reimburse the trust funds on a current basis for the employer-employee taxes (OASDHI) on additional military wage credits given for non-cash compensation.

Trust fund investment procedure

Provide for reinvesting all trust fund assets each month at a rate of interest based on the average market rate on all public-debt obligations currently held by Treasury with a duration of four or more years until maturity.

Public members on board of trustees

Add two public members to the Board of Trustees of the OASDI, HI, and SMI trust funds. The public members would be nominated by the President and confirmed by the Senate. The two public members could not be from the same political party. Public members shall not be considered fiduciaries and shall not be personally liable for any actions taken in such capacity with respect to the trust funds.

Accelerate State and local deposits

Apply the same social security tax deposit requirements to State and local governments that presently apply to private employers.

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Triggered normalization of tax transfers

When, at the start of any month, the Secretary of the Treasury determines that the reserves of the OASDI trust funds are inadequate to meet 1½ months of benefits, the Secretary would be required to credit the trust funds on the first day of the next month with the full payroll tax revenues estimated for the month. Interest would be paid to the General Treasury.

Social security wage base

Expand the social security wage base to include certain deferred compensation.

SUMMARY OF SUPPLEMENTAL SECURITY INCOME SSI PROVISIONS

Delay the SSI COLA and increase the SSI disregard

Delay the annual cost-of-living adjustment (COLA) for SSI payments from July to January, beginning with the July 1983 benefit increase, thereby maintaining the link between the COLA for SSI and OASDI. In addition, increase the SSI payment standard applicable to all individuals by $20 ($30.00 for a couple) per month, effective July 1983. To help protect the States from increased costs resulting from this provision, expand current law to allow States to meet the "pass through" requirement for 1983 if they pass through the equivalent of the COLA that would have occured under current law rather than the proposed monthly payment increase.

SSI alert

Require the Secretary of Health and Human Services to notify elderly OASDI recipients of the availability of SSI and to encourage those potentially eligible to contact their district offices.

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TITLE I OF THE BILL

A. Provisions Related to Old-Age, Survivors and Disability Insurance

COVERAGE OF NEWLY HIRED FEDERAL EMPLOYEES

(Section 101 of the Bill)

Present law

Approximately 91 percent of the Nation's workers are covered by social security. Federal civilian employees are the only major group excluded from coverage under the social security (OASDI) system. Those excluded (93 percent, or about 2.6 million out of 2.8 million employees) are generally covered by a Federal staff retirement system, engaged in temporary employment, or are members of Congress. (Beginning in 1983, nearly all Federal employees are covered under Medicare.)

Committee amendment

The Committee amendment would, effective January 1, 1984, extend social security coverage to all Federal civilian employees hired after 1983 (unless their break in Federal service has been one year or less), and to all current members of Congress, the President, Vice President, the Social Security Commissioner, and to current Congressional staff not already covered under a Federal staff retirement system.

This amendment is similar to the recommendation of the National Commission on Social Security Reform to extend coverage to all Federal employees hired after 1983.

The Committee amendment also states that "Nothing in this Act shall reduce the accrued entitlement to future benefits under the Federal retirement system of current and retired Federal employees and their families."

Effective date.—January 1, 1984.

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REVENUE GAIN

[in billions, calendar years]

	1984	1985	1986	1987	1988	1989	1983-89
Short-range	$0.2	$0.7	$1.2	$1.8	$2.4	$3.1	$9.3
Long-range: 0.28 percent of taxable payroll.							

COVERAGE OF NONPROFIT EMPLOYEES

(Section 102 of the Bill)

Present law—Work performed for a nonprofit tax-exempt organization (specified in section 501(c)(3) of the Internal Revenue Code of 1954) is excluded from social security coverage unless the organization files a certificate with the Internal Revenue Service waiving its exemption from social security taxes. Nonprofit organizations may terminate coverage upon giving 2 years advance notice, providing coverage has been in effect for 8 years or more. Once coverage has been terminated, the organization cannot again cover its employees. About 4.3 million employees of nonprofit organizations (about 80 percent) are covered.

Committee amendment—The Committee amendment would extend social security coverage on a mandatory basis to all employees of nonprofit organizations.

This amendment is the same as the recommendation of the National Commission on Social Security Reform.

Effective date—January 1, 1984.

OASDI REVENUE GAIN

[in billions, calendar years]

	1984	1985	1986	1986	1987	1988	1983–89
Short-range	$1.3	$1.5	$1.8	$2.1	$2.6	$3.1	$12.5
Long-range: .10 percent of taxable payroll.							

PROHIBIT WITHDRAWAL OF STATE AND LOCAL EMPLOYEES

(Section 103 of the Bill)

Present law

Employees of State and local governments may be covered under social security at the option of the State and in agreement with the Secretary of Health and Human Services. Coverage may be terminated if the State gives 2 years written notice of such intent, provided that the State or local group has been covered for at least 5 years. Once coverage is terminated, the group can never again be covered under social security.

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Committee Amendment

The Committee amendment would prohibit State and local governments from terminating coverage for their employees. Pending terminations would be invalid, effective on enactment. In addition, the amendment would provide an opportunity for State and local governments which have withdrawn from the social security system to voluntarily rejoin. Once having rejoined, the governmental entity would be precluded from terminating coverage.

This amendment is similar to the recommendation of National Commission on Social Security Reform.

Effective date.—On enactment.

OASDI REVENUE GAIN

[In billions, calendar years]

	1984	1985	1986	1987	1988	1989	1983–89
Short-range	$0.1	$0.2	$0.4	$0.6	$0.8	$1.1	$3.2
Long-range: .06 percent of taxable payroll.							

Exclusion from social security coverage for services performed by members of certain religious sects (sec. 104 of the bill and sec. 3121 of the Code)

PRESENT LAW

In general, social security (FICA) tax is imposed on every individual who receives wages with respect to employment. In addition, social security tax is imposed on employers who pay wages with respect to employment. There is no exemption, under present law, for employers or employees who are members of religious sects that oppose the social security system. However, present law does provide an exemption from self-employment tax (SECA) for members of religious sects that are conscientiously opposed to the acceptance of private or public insurance and which make provision for the care of their dependent members.

REASON FOR CHANGE

The committee believes that employers and employees who are members of the Amish sect, or other religious sects that oppose participation in the social security system, should be treated the same as self-employed members of those sects. That is neither Amish employers nor Amish employees should be required to pay social security taxes. This provision is necessary because, due to economic conditions, many Amish members cannot afford their own farms, but, rather, must work for other Amish farmers.

EXPLANATION OF PROVISION

The provision will exempt from social security tax wages paid by individuals who are exempt from self-employment taxes because of their religious beliefs to individuals who are members of religious sects that conscientiously oppose the acceptance of private or

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public insurance and which make provisions for the care of their dependent members. This exemption applies both to the employer and employee portion of social security tax.

The exemption applies only in the case of religious sects that have been in existence at all times since December 31, 1950.

EFFECTIVE DATE

The provision applies to remuneration paid after December 31, 1983.

DELAY COST-OF-LIVING ADJUSTMENT TO A CALENDAR YEAR BASIS

(Section 111 of the Bill)

Present law

The automatic cost-of-living adjustment (COLA) of social security benefits is applicable to June benefits (payable early in July). The amount of the increase is equal to percentage by which the Consumer Price Index (for Urban Wage Earners and Clerical Workers, CPI–W) for the first quarter of the calendar year has increased over the CPI for the first quarter of the previous calendar year. No COLA is paid unless the increase in the CPI is at least 3 percent. By law, cost-of-living adjustments in the SSI program are made at the same time, and in the same amount as the social security cost-of-living adjustment.

Committee amendment

The Committee amendment would shift the automatic cost-of-living adjustment of social security benefits to a calendar year basis. Beginning in 1983, the COLA for OASDI benefits would be applied to the December benefit, which is payable at the beginning of January. For 1983, the COLA would be calculated as under current law (i.e., the change in the CPI for the first quarter of 1983 over the CPI for the first quarter of 1982). Beginning with the COLA for 1984, the adjustment would be computed by comparing the increase in the CPI for the third quarter of a year over the CPI for the third quarter of the previous year. This would ensure that the lag between the end of the period over which the COLA is measured and the time the COLA is actually applied to benefits remains 3 months. This is the same proposal recommended by the National Commission on Social Security Reform.

In addition, the Committee amendment would, for 1983 only, provide the COLA even if it is less than 3 percent. The SMI (Supplemental Medical Insurance) premium increase would also be shifted to a calendar year basis.

Under the Committee amendment, the SSI COLA would also be shifted to a calendar year basis and would be measured in the same way as for OASDI purposes.

Effective date.—For cost of living adjustment otherwise payable in July 1983 checks.

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OASDI SAVINGS

[In billions, calendar years]

	1983	1984	1985	1986	1987	1988	1989	1983–89
Short range	$3.2	$5.2	$5.4	$5.5	$6.2	$6.7	$7.3	$39.4
Long range: .30 percent of taxable payroll.								

SST COSTS (CBO ESTIMATES)

[In millions, fiscal years]

	1983	1984	1985	1986	1987	1988
Costs	–$100	–$130	–$170	–$170	–$175	–$210

ELIMINATE "WINDFALL" BENEFITS

(Section 112 of the Bill)

Present law

Social security benefits for workers with low average earnings are a relatively high proportion (up to 90 percent) of their average earnings under social security. No distinction is currently made between persons who have a lifetime of low earnings and those who have low average earnings only because they worked few years in covered employment (possibly at high wages) and many years in employment not covered by social security. Both groups receive the heavily weighted social security benefit intended for the first group. The heavily weighted benefit paid to the second group is often referred to as a "windfall".

The present law benefit formula for persons who reach age 62 or who become disabled before age 62 in 1983 is: 90 percent of the first $254 of average indexed monthly earnings in covered employment (AIME), plus 32 percent of AIME over $254 and up to $1,528, plus 15 percent of AIME in excess of $1,528.

Committee amendment

The Committee amendment would reduce (but not eliminate) social security benefits for retired and disabled workers who first become eligible for a pension based on non-covered employment after 1983. For such workers who do not have a long record of substantial work under social security, the heavily weighted 90 percent factor in the benefit formula would be replaced by a factor of 32 percent, phased in over a five year period as follows:

Benefit factor

Year of first eligibility under OASDI:	*Percent*
1984	78.4
1985	66.8
1986	55.2
1987	43.6
1988 and after	32.0

To moderate the impact of this provision on people with small pensions from non-covered employment, social security benefits

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could in no case be reduced by more than one-third of the portion of the worker's pension based on service which was non-covered employment. The offset would not apply to persons with pensions based on one year or less of non-covered employment.

In addition, the Committee amendment exempts from any reduction under this provision those individuals who have a long history of substantial work under the social security program. People who have thirty or more years of covered employment in which they paid social security taxes on at least 25 percent of the maximum taxable earnings would have their benefits computed under the regular provisions without any reduction under the windfall provision. People with less than 30 but more than 24 years of substantial social security employment would have the windfall reduction applied on a phased in basis under which the first factor in the benefit formula would be reduced by 10 percentage points for each year below thirty years of covered employment. This would not reduce benefits by more than the regular windfall provision however. (A year of substantial employment is a year in which covered earnings were at least 25 percent of the wage base. For years after 1977, the base used would be the 1977 base with adjustments for increased earnings after that date.)

Survivor benefits would not be affected by this provision.

The National Commission on Social Security Reform recommended modifying the social security benefit formula so as to eliminate windfall benefits received by workers who in the future receive social security as well as pensions from non-covered employment. (No specific formula was recommended.)

Effective date.—January 1, 1984, for retired or disabled workers who first become eligible for a non-covered pension after 1983.

OASDI SAVINGS

[In billions, calendar years]

	1984	1985	1986	1987	1988	1989	1984–89
Short range	([1])	([1])	([1])	([1])	$0 1	$0.1	$0 3
Long range .05 percent of taxable payroll.							

[1] Less than $50 million.

BENEFITS FOR DIVORCED OR DISABLED WIDOWERS OR WIDOWS WHO REMARRY

(Section 113 of the Bill)

Present law

Current law permits the continuation of benefits for widows and widowers who remarry after age 60, the age of first eligibility for benefits. If the widow(er) marries after age 60, he or she receives the benefits to which he or she is entitled as a wage earner, widow(er) or spouse, whichever is larger. However, benefits for disabled widow(er)s and disabled surviving divorced spouses (payable from age 50 to 60) and for surviving divorced spouses (payable at age 60) are terminated if the individual remarries.

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Committee amendment

The Committee amendment would provide that benefits continue to be paid to certain beneficiaries upon remarriage if that marriage takes place after the age of first eligibility. Benefits would be payable to: disabled widow(er)s and disabled surviving divorced spouses who remarry after age 50, and surviving divorced spouses who remarry after 60. No change would be made in the current dual entitlement provision of the law which allows only the highest benefit to which an individual is eligible to be drawn. This is comparable to the present law treatment of widows and widowers.

This amendment is the same as the recommendation of the National Commission on Social Security Reform.

Effective date.—For benefits payable for months after December 1983.

OASDI COST

[In billions, calendar years]

	1984	1985	1986	1987	1988	1989	1984–89
Short range	(1)	(1)	(1)	(1)	(1)	(1)	−$0.1
Long range: negligible.							

1 Less than $50 million.

CHANGES IN INDEXING FOR DEFERRED SURVIVOR BENEFITS

(Section 114 of the Bill)

Present law

Survivor benefits (for widows, widowers, and surviving children) are based on the deceased worker's earnings in covered employment. Such earnings are indexed to reflect economy-wide wage increases through the second year before the death of the worker. Beginning with the year of death, benefit levels are indexed to price changes.

Should the worker die long before the spouse is eligible for benefits, the benefit to which the widowed spouse ultimately becomes eligible (in old-age or at disability) is based on outdated wages. Thus, women who become widowed at a relatively young age, but do not become eligible for benefits for many years, are deprived of their husband's unrealized earnings as well as the economy-wide wage increases that may have occurred since the death of their husbands.

Committee amendment

The Committee amendment would provide that deferred widow and widower benefits would continue to be based on earnings indexed to wages as under present law, however, this wage indexing would continue after the death of the worker. This is the same as the recommendation of the National Commission on Social Security Reform. In addition, the Committee amendment would specify that such wage indexing would apply through the year the worker would have reached age 60, or two years before the survivor be-

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comes eligible for aged or disabled widow's benefits, whichever is earlier. In no case would benefits be lower than under present law.

Effective date.—For persons becoming eligible for survivors benefits after December 31, 1984.

OASDI COST

[In billions, calendar years]

	1984	1985	1986	1987	1988	1989	1984 89
Short range		(1)	(1)	(1)	(1)	(1)	(1)
Long range: —.05 percent of taxable payroll.							

[1] Less than $50 million.

INDEPENDENT ELIGIBILITY FOR DIVORCED SPOUSES

(Section 115 of the Bill)

Present law

A divorced spouse, eligible for benefits at age 62, may not begin to draw social security benefits until the worker begins to draw benefits. For some divorced women, this means that they may have to wait several years beyond their own retirement age (either because their ex-spouse delays retirement or otherwise fails to apply for benefits) before they can begin to draw benefits.

Committee amendment

The Committee amendment would allow divorced spouses (who have been divorced for a significant period) to draw benefits at age 62 if the former spouse is eligible for retirement benefits, whether or not the former spouse has claimed these benefits or has had them suspended because of substantial employment. This is the same as the recommendation of the National Commission on Social Security Reform. In addition, the Committee amendment would specify that the proposal would only apply to spouses who have been divorced for at least two years.

Effective Date—For benefits payable for months after December 1984.

OASDI COST

[In billions, calendar years]

	1984	1985	1986	1987	1988	1989	1983–89
Short range		(1)	(1)	(1)	(1)	(1)	-$0.1
Long range: —.01 percent of taxable payroll.							

[1] Less than $50 million.

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INCREASE BENEFITS FOR DISABLED WIDOWS AND WIDOWERS

(Section 116 of the Bill)

Present law

Social Security benefits for widows and widowers are first payable at age 60. Benefits are payable in full (i.e., 100 percent of the worker's primary insurance amount) at age 65, and at reduced rates at ages 60–64 (i.e., phasing up from 71.5 percent of the primary insurance amount at age 60). Benefits also payable at reduced rates to disasbled widows and widowers aged 50–59 (i.e., phasing up from 50 percent of the primary insurance amount at age 50).

Committee amendment

The Committee amendment would increase benefits for disabled window(er)s age 50–59 to 71.5 percent of the primary insurance amount, the amount to which widow(er)s are entitled at age 60. The proposal would be applicable to new beneficiaries and to those on the rolls on the effective date of the provision. This is the same as the recommendation of the National Commission on Social Security Reform.

Effective date.—For benefits payable for months after December 1983.

OASDI COST

[In billions, calendar years]

	1984	1985	1986	1987	1988	1989	1984–89
Short range	−$0.2	−$0.2	−$0.2	−$0.2	−$0.3	−$0.3	−$1.4
Long range: −.01 percent of taxable payroll.							

ADJUSTMENT OF COST-OF-LIVING INCREASE WHEN TRUST FUND RATIO FALLS BELOW 20 PERCENT

(Section 117 of the Bill)

Present law

The automatic cost-of-living adjustment (COLA) in social security benefits is applicable to the June benefit, which is payable at the beginning of July, and is based on the increase in the Consumer Price Index. When increases in prices outrun increases in wages, income to the trust funds falls behind outgo, and cash flow problems may result. There is no mechanism under current law to adjust trust fund outlays and revenues to take account of such adverse economic fluctuations.

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Committee amendment

The Committee amendment would modify the cost-of-living adjustment formula during periods when trust fund reserves are low in order to help stabilize reserves. Specifically, if the OASDI trust fund ratio (reserves as a percentage of outgo) as of the beginning of a year is less than 20 percent, the adjustment of OASDI benefits would be based on the lower of the increase in the CPI or average wages. Subsequently, when the balance in the trust funds has risen to at least 32 percent of estimated annual outlays, "catch-up" benefit payments would be made during the following year, but only to the extent that sufficient funds are available over those needed to maintain a fund ratio of 32 percent. Catch-up payments would supplement monthly benefits otherwise payable to make up for any COLA losses that result from basing the adjustment on wages rather than prices. This would not apply to the COLA for the Supplemental Security Income (SSI) program. This is the same as the recommendation of the National Commission on Social Security Reform.

Effective date.—This provision would first be applicable in 1988.

Cost/savings.—This proposal is estimated to have no impact on the trust funds under 1983 Trustees II-B assumptions.

INCREASE DELAYED RETIREMENT CREDIT

(Section 118 of the Bill)

Present law

A worker who delays retirement beyond age 65 (i.e., does not actually receive social security benefits) is eligible for a delayed retirement credit (DRC). The worker's benefit is increased for each month after age 65 and prior to age 72 for which benefits are not paid, either because of earnings or because the worker does not claim benefits. for workers eligible for benefits after 1978, the DRC is equal to 3 percent per year (one-quarter of 1 percent per month).

Committee amendment

The Committee amendment would gradually increase, between 1990 and 2010, the delayed retirement credit to 8 percent per year, as recommended by the National Commission on Social Security Reform. (The amount of credit would relate to year of attainment of age 65.) Beginning in 1990 the DRC would be increased by ¼ percent each subsequent year until reaching 8 percent in 2010.

OASDI cost: -0.10 percent of taxable payroll.

INCREASE IN RETIREMENT AGE

(Section 119 of the Bill)

Present law

Unreduced retirement benefits are available to workers, spouses, and widows and widowers at age 65. Actuarially reduced benefits are available at age 62 for workers and spouses and at age 60 for widows and widowers.

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Committee amendment

The Committee amendment would gradually raise the age at which full social security benefits are payable from 65 to 66, beginning with those who attain age 62 in 2000. Under this provision, the normal retirement age would be increased one month per year, reaching 66 for those attaining 62 in the year 2012 or later. Early-retirement benefits would continue to be available beginning at age 62 for workers and spouses and at age 60 for widows and widowers, but the actuarial reduction factors would be larger. The minimum age for eligibility for medicare benefits would continue to be tied to the age at which unreduced retirement benefits are first available.

The majority of the members of the National Commission on Social Security Reform made this recommendation. In addition, they recommended indexing the retirement age to changes in longevity, beginning in 2012.

Effective date.—For people attaining 62 in 2000.

OASDI savings: 0.40 percent of taxable payroll.

LONG-RANGE BENEFIT CHANGE

(Section 120 of the Bill)

Present law

In computing social security benefits, a worker's earnings under social security are averaged and a benefit formula is applied to those average indexed monthly earnings (AIME) to arrive at the initial basic benefit amount called the primary insurance amount (PIA). The PIA is the amount a worker is eligible to receive at 65. Dependents' and survivors' benefits are based on the worker's PIA.

The formula for a worker who becomes eligible for benefits in 1983 is: 90 percent of the first $254 of AIME, plus 32 percent of the AIME from $254 through $1,528, plus 15 percent of the AIME over $1,528.

The two dollar figures in the formula, $254 and $1,528, are raised (indexed) each year to reflect increases in average wages in the economy. Thus, a new formula is created each year for the new group of workers becoming eligible for benefits in that year.

This system was adopted by the 1977 Social Security Amendments. The annual adjustment of the dollar amounts in the benefit formula, the bend points, by the full amount of the increase in average wages leads to higher initial benefits over time and to replacement rates—the percentage of a worker's prior earnings that are replaced by his social security benefit—that remain at approximately the same level.

Committee amendment

For people first becoming eligible for benefits in 2000, the Committee amendment would reduce initial benefit levels by 5.3 percent by decreasing the percentage factors in the benefit formula by two-thirds of one percent each year for 8 years. This would have the effect of reducing the ultimate replacement rate by 5 percent.

Effective date.—For people first becoming eligible for retirement or disability in 2000.

OASDI savings: 0.43 percent of taxable payroll.

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ELIMINATION OF RETIREMENT EARNINGS TEST

(Section 121 of the Bill)

Present law

Social security beneficiaries under age 70 who work and have earnings are subject to a one dollar reduction in benefits for every two dollars of earnings, when their earnings exceed certain exempt amounts. For 1983, the annual exempt amount is $6,600 for people age 65 and older.

Committee amendment

The Committee amendment would gradually phase out, between 1990 and 1994, the retirement earnings test for people 65 and older. The exempt amount of earnings would be increased by $3,000 in 1900 and in each of the next four years, with the earnings test (for people 65 and older) completely eliminated in 1995.

Effective date.—The provision would be phased in between 1990 and 1994.

OASDI cost.—This amendment is estimated to cost 0.05 percent of taxable payroll in the long-range.

CHILD-CARE DROP OUT YEARS

(Section 122 of the Bill)

Present law

In computing a worker's covered earnings history under social security (upon which his and his family's benefits are based), up to five years in which earnings are lowest are dropped.

Committee amendment

The Committee amendment would allow up to two additional years to be dropped for persons who leave the workforce to care for a child under 3 in the home. To qualify for a child-care drop year, the worker can have no earnings at all during the year.

Effective date.—For persons first eligible for benefits after 1983.

OASDI COST

[In billions, calendar years]

	1984	1985	1986	1987	1988	1989	
Short-range:	([1])	−$0.1	−$0.1	−$0.2	−$0.4	−$0.5	−$1.3
Long range: −.04 percent of taxable payroll.							

[1] Less than $50 million.

PRISONERS BENEFITS

(Section 123 of the Bill)

Present law

Persons imprisoned for the conviction of a felony may not receive student benefits (which are being phased out anyway), and are not

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eligible for disability benefits unless they are participating in a court-approved rehabilitation program. (Dependents benefits are not affected.) Also, impairments resulting from the commission of a crime cannot be the basis for disability benefits and impairments occurring during imprisonment cannot be the basis for disability benefits during the period of imprisonment.

Presently, benefits may continue to be paid to incarcerated felons who are either retired workers, widow or widower beneficiaries, spouses of retired or disabled workers, and to those DI beneficiaries in a court-approved rehabilitation program.

Committee amendment

The Committee amendment would expand present law to eliminate all benefits to felons during their period of incarceration. Benefits of dependents and survivors of incarcerated felons would not be affected.

Effective date.—Applicable to benefits paid for the month after enactment.

OASDI Cost: Negligible.

ELIMINATE BENEFITS TO ALIENS

(Section 124 of the Bill)

Present law

There are no citizenship or residence requirements for receiving social security cash benefits (OASDI). Any alien in the U.S.—whether legally or illegally, or as a permanent or temporary resident—is eligible for benefits provided he has engaged in covered employment and otherwise meets the eligibility requirements. Dependents and survivors are also eligible for benefits regardless of their immigration status or that of the insured worker.

About $1 billion is being paid annually to the 314,000 beneficiaries who reside abroad. About 70% of these beneficiaries are aliens.

Committee amendment

The Committee amendment provides that, in the future, benefits would be eliminated to alien workers, their dependents and survivors who reside abroad. No benefits would be paid to alien dependents of alien workers who were acquired (through marriage, birth or adoption) while outside the United States. However, benefits would be paid under the following conditions:

(1) the worker is the citizen of a country with which the United States has a treaty or totalization agreement which provides for reciprocity of social security coverage; and

(2) benefits would continue until total benefits paid to the wage earner and dependents equal taxes paid by the wage earner.

Effective dates.—This amendment would apply to new eligibles on or after January 1, 1985.

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OASDI SAVINGS

[Dollars in billions, calendar years]

	1983	1984	1985	1986	1987	1988	1989	1983-89
Short range	(1)	(1)	(1)	(1)	(1)	(1)	(1)	(1)
Long range: .01 percent of taxable payroll.								

[1] Savings of less than $50 million.

FAIL-SAFE PROVISION

(Section 125 of the Bill)

Present law

Presently, there are no "fail-safe" provisions in the social security system that ensure benefit payments can be met on an ongoing basis in the face of adverse economic conditions. (The Board of Trustees is required to report immediately to the Congress if any of the trust funds is "unduly small".)

Committee amendment

Under the Committee amendment, the Secretary of Health and Human Services would be required to make an annual evaluation of the projected balances in the cash benefits trust funds, taking into account future cost-of-living increases. If the cash benefits (OASDI) fund reserves are projected to decline from the start of the next year to the start of the following year and to then be less than 20 percent of a year's benefits, the Secretary would be required to notify the Congress and if no action is taken, to scale back the COLA to the extent necessary to prevent a decline which would leave the reserves below that level.

Insofar as possible, the limitation on the COLA would be applied to people whose benefits are based on a primary benefit level of more than $250 per month. The determination as to whether a limitation on the cost-of-living increase was necessary would be made only after taking into account all other statutory provisions for assuring adequate funds. The Secretary would have to notify Congress by July 1 of each year in which he finds that action to limit the next cost-of-living increase would be required under this provision. Since cost-of-living increases will be reflected in the January checks, this would give Congress several months in which to provide additional funding or to address the problem in any other manner the Congress might find to be appropriate.

The Committee views this provision as a last resort which would come into play only after all other authorities for maintaining trust fund solvency had been exercised. Thus, for example, other provisions in this legislation for such procedures as interfund borrowing and normalization of tax transfers would be invoked before this provision would be operative to the extent that such procedures are authorized by law. Under current projections such measures should be sufficient to keep fund balances from declining to dangerous levels. If, however, unexpected adverse situations should develop, this provision would assure that sufficient reserves were

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maintained so that regular, timely payment of monthly benefit checks would not be placed in jeopardy.

This provision would implement the recommendation of the National Commission on Social Security Reform that this social security financing legislation include provision for a "fail-safe" mechanism.

Effective date.—Determinations beginning July 1, 1984.

OASDI Cost Impact: This provision is not expected to be utilized under the 1983 Trustees intermediate (II-B) assumptions.

PART C—REVENUE PROVISIONS

A. Taxation of social security and railroad retirement benefits (sec. 131 of the bill, new Code secs. 86 and 6050, and Code secs. 861, 871, 1441, and 6103)

Present law

Under present law, social security benefits are excluded from the gross income of the recipient. Their exclusion is based upon a series of administrative rulings issued by the Internal Revenue Service in 1938 and 1941 (see I.T. 3194, 1938-1 C.B. 114, I.T. 3229, 1938-2 C.B. 136, and I.T. 3447, 1941-1 C.B. 191). Railroad retirement benefits are excluded from gross income under the Railroad Retirement Act.

In general, the gross amount of fixed or determinable annual or periodic income (which is not effectively connected with a U.S. trade or business) received by a nonresident alien from U.S. sources is subject to a 30-percent tax (Code sec. 871); this tax is collected by withholding (sec. 1441). A pension for services performed in the United States would be U.S.-source income and the gross amount of a U.S.-source pension is subject to the 30-percent withholding tax or a lower rate if so provided by treaty. The U.S. Model Income Tax Treaty, as well as a number of actual tax treaties to which the United States is a party, provides reciprocally that pensions received by a resident of one country from sources in the other country are taxable only by the country of residence. However, the United States has reserved the right to tax social security benefits in the U.S. Model Income Tax Treaty and a number of actual tax treaties.

Reasons for change

The Committee believes that the present policy of excluding all social security benefits from a recipient's gross income is inappropriate. The committee believes, further, that social security benefits are in the nature of benefits received under other retirement systems, which are subject to taxation to the extent they exceed a worker's after-tax contributions and that taxing a portion of social security benefits will improve tax equity by treating more nearly equally all forms of retirement and other income that are designed to replace lost wages (for example, unemployment compensation and sick pay). Furthermore, by taxing social security benefits and appropriating these revenues to the appropriate trust funds, the financial solvency of the social security trust funds will be strengthened.

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Because Tier 1 benefits provided under the Railroad Retirement Act are largely equivalent to social security benefits, the committee believes that corresponding changes also should be made in the tax treatment of these benefits. That is, a portion of railroad retirement benefits also should be subject to income taxation.

By taxing only a portion of social security and railroad retirement benefits (that is, up to one-half of benefits in excess of a certain base amount), the Committee's bill assures that lower-income individuals, many of whom rely upon their benefits to afford basic necessities, will not be taxed on their benefits. The maximum proportion of benefits taxed is one-half in recognition of the fact that social security benefits are partially financed by after-tax employee contributions. The bill's method for taxing benefits assures that only those taxpayers who have substantial taxable income from other sources will be taxed on a portion of the benefits they receive.

Taxation of social security and railroad retirement benefits

Under the committee's bill, a portion of social security benefits will be included in the gross income of recipients whose adjusted gross income exceeds certain levels. (This provision is not intended to change the tax treatment of social security benefits paid by foreign governments; these benefits have been held by Treasury to be fully includible in gross income (Rev. Rul. 62–1979, 1962–2, C.B. 20)). The bill defines a "social security benefit" as any amount received by the taxpayer by reason of entitlement to either (1) a monthly benefit under title II of the Social Security Act (Federal Old-Age, Survivors, and Disability Insurance Benefits (OASDI)), or (2) Tier 1 benefit under the Railroad Retirement Act of 1974. A Tier 1 benefit generally is a monthly benefit equal to what an individual would receive if the formula for computing social security benefits were applied to the individual's history of covered wages under both the social security and railroad retirement systems.

Social Security benefits, to the extent they are taxable, will be included in the taxable income of the person who has the legal right to receive the benefits. For example, benefits paid to a child (or on behalf of a child under section 203(i) of the Social Security Act) will be considered to be the child's and will be added to the child's other income to determine whether they are taxable. The amount of benefits received refers to benefit payments after reductions under such provisions as actuarial reductions, family maximum, and the earnings test, but includes certain amounts that may be withheld from benefits, such as payments of supplementary medical insurance premiums, where the amounts withheld are for the purpose of meeting a financial obligation incurred by the individual entitled to receive such benefit payments. In addition, the amount of any social security benefits received will include the total amount of the benefits without any reduction for attorneys' fees, if any, paid in order to enable an individual to receive those benefits. The committee expects the Secretary of the Treasury to provide guidance on the extent to which expenses (such as attorneys' fees) incurred in perfecting claims to social security benefits may be deducted, now that some of the social security benefits may be taxed.

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Social security benefits that will be included in the gross income of a taxpayer for a taxable year will be limited to the lesser of (1) one-half of the social security benefits received, or (2) one-half of the excess of the sum of the taxpayer's adjusted gross income, interest on obligations exempt from tax, and one-half of the social security benefits received, over the appropriate base amount. Thus, the maximum proportion of social security benefits that will be included in the gross income of any taxpayer will be one-half of benefits. This provision does not affect the exclusion for interest on tax-exempt obligations. Rather, it merely includes that interest in the base for the purpose of determining the amount of an individual's social security benefits that will be taxed.

The base amount is $32,000 in the case of a married individual filing a joint return; zero in the case of a married individual filing a separate return, unless he or she lived apart from his or her spouse for the entire taxable year; and $25,000 in the case of all other individuals.

The base amount is zero for married individuals filing separate returns because the committee believes that the family should be treated as an integral unit in determining the amount of social security benefit that is includible in gross income under this provision. If the base amount for these individuals were higher, couples who are otherwise subject to tax on their benefits and whose incomes are relatively equally divided would be able to reduce substantially the amount of benefits subject to tax by filing separate returns.

For the purpose of determining how much of a taxpayer's social security benefit will be included in gross income, a taxpayer will be permitted to reduce benefits received during the taxable year by the amount of benefits, previously received during the current or any preceding taxable year, that he repays during the taxable year. This provision is necessary to prevent a taxpayer from being subject to taxation on his benefits in those situations in which a taxpayer must repay a portion of those benefits because he has been overpaid previously. A taxpayer will be permitted an itemized deduction, to the extent allowed under section 165, for repayments of social security benefits which had been included in gross income in a previous year, to the extent that the repayments exceed social security benefits received by the taxpayer, and not repaid, during the taxable year. Alternatively, if such amount repaid exceeds $3,000, the taxpayer has the option under section 1341 to compute tax for the taxable year without the deduction and to subtract from that amount the reduction in tax that would have resulted from excluding the amount repaid from income for the year of the overpayment.

The committee's bill provides an elective, special rule for taxpayers who receive lump-sum payments. This rule was determined to be necessary because in some situations involving lump-sum payments of benefits attributable to prior years, the general income-aveaging rules may not provide adequate relief.

If this special rule is elected, the taxpayer will detemine the tax for the taxable year of receipt of the lump-sum payment by including in gross income for the current year the sum of the increases in gross income that result solely from taking into account the appro-

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priate portions of the lump-sum payment in the taxable year to which they are attributable. The committee intends that when lump-sum payments are made, the Social Security Administration or Railroad Retirement Board will notify the recipients thereof of the taxable years to which the payments are attributable.

Social security benefits are to be treated as a pension or annuity and, therefore, not treated as earned income, for purposes of the earned income credit, the deduction for contributions to individual retirement arrangements, the deduction for two-earner couples, and the foreign earned income exclusion.

Returns relating to social security benefits

Information reporting will be required with respect to benefit payments. Specifically, the appropriate Federal official (*i.e.*, the Secretary of Health and Human Services, in the case of social security benefits, and the Railroad Retirement Board, in the case of railroad retirement benefits) will be required to report to the Treasury (1) the aggregate amount of benefits paid with respect to any individual during any calendar year; (2) the aggregate amount of benefits repaid by the individual during the calendar year; and (3) the name and address of the individual with respect to whom benefits are paid. In addition, each individual receiving social security or railroad retirement benefits will be furnished with a written statement showing (1) the name of the agency making the payments, and (2) the aggregate amount of payments and repayments. This statement will be due by January 31 of the year following the year in which social security benefits are paid.

Treatment of nonresident aliens

The committee's bill provides that social security benefits paid by the United States are U.S.-source income for purposes of the Code, including the foreign tax credit. In addition, one-half of social security benefits paid to nonresident aliens will be subject to the general 30-percent tax which will be collected by withholding. The committee's bill is not intended to override the treatment of social security benefits provided in existing income tax treaties to which the United States is a party.

The committee's bill permits the Secretary of the Treasury to disclose to the Social Security Administration or the Railroad Retirement Board available return information from the master files of the Internal Revenue Service with respect to the address and status of an individual as a nonresident alien or as a resident or citizen of the United States. This information, which may be disclosed upon written request, may be disclosed to the Social Security Administration and the Railroad Retirement Board only for purposes of carrying out their responsibilities for withholding taxes from social security benefits of nonresident aliens. Any return information disclosed under this provision will be subject to the present law requirements regarding recordkeeping and safeguarding of return information.

Transfers to trust funds

The committee's bill appropriates to each payor fund the increase in Federal income tax liabilities attributable to taxing social

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security benefits. This amount is the difference between total income tax liabilities for the year and what income tax liabilities would have been without the application of the Code sections which provide for the taxation of benefits. A "payor fund" is any trust fund or account from which payments of social security benefits are made.

The appropriated amounts are to be transferred from time to time (but no less frequently than quarterly) from the general fund of the Treasury on the basis of estimates made by the Secretary of the Treasury. Transfers to the payor funds may be based on the proportion of each type of benefit as a share of the total benefits potentially includible in gross income under these provisions. For example, suppose that after adding OASI benefits, DI benefits and Tier I railroad retirement benefits the shares of these in the total are 80 percent, 16 percent, and 4 percent, respectively. These percentages of the increase in tax liabilities described above may then be transferred to the respective funds.

Any quarterly payment to a payor trust fund must be made on the first day of the quarter and must take into account social security benefits estimated to be received during the quarter. Proper adjustments are to be made in the amounts subsequently transferred to the extent that prior estimates were in excess of, or less than, the amounts required to be transferred. A final determination of the amount required to be transferred for a year may be based on an estimate derived from the appropriately weighted sample of individual income tax returns for that year which is used as the basis for the Internal Revenue Service's publication of statistics of income for that year under Code section 6108. In making these estimates, the Secretary of the Treasury need not take account of certain provisions of the tax law that might affect an individual's tax liability (*e.g.,* income averaging, loss carrybacks, etc.) if these provisions are judged to have an inconsequential effect on the estimates.

The Secretary of the Treasury will be required to submit annual reports to the Congress and to the Secretary of Health and Human Services and the Railroad Retirement Board concerning (1) the transfers made during the year, and the methodology used in determining the amount of the transfers and the funds or account to which made, and (2) the anticipated operation of the transfer mechanism during the next five years.

Taxation of Tier One railroad retirement benefits

The Committee's bill provides that railroad retirement "Tier 1" benefits are subject to taxation to the same extent and in the same manner as monthly benefits payable under title II of the Social Security Act. As a result of this change, certain amounts will be transferred regularly to the Railroad Retirement Account.

Under the financial interchange between railroad retirement and social security, however, the social security trust funds are placed in the same position they would have been in if railroad employment were covered under social security. Therefore, the committee understands that existing law requires that the proceeds of income taxes on those railroad retirement benefits which are strictly equivalent to social security benefits are to be credited to the

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social security trust funds through adjustments in the financial interchange. This will produce exactly the same result as if the social security system had paid that portion of the tier I benefits which are strictly equivalent to social security benefits and had received the proceeds of the income tax on these benefits.

Effective date

In general, the provisions will apply to benefits received after December 31, 1983, in taxable years ending after that date. However, the provisions will not apply to benefits received after December 31, 1983, if the generally applicable payment date of these benefits was before January 1, 1984.

B. Acceleration of increases in FICA taxes; 1984 employee tax credit (sec. 132 of the bill; secs. 3101, 3111, and new sec. 3510 of the code)

Present Law

Under present law, several increases in social security payroll tax (FICA) rates are already scheduled to take effect between 1985 and 1990, as shown in the following table:

EMPLOYER-EMPLOYEE RATE (EACH)

Year	OASDI	HI	OASDI-HI
1984	5.4	1.30	6.70
1985	5.7	1.35	7.05
1986	5.7	1.45	7.15
1987	5.7	1.45	7.15
1988	5.7	1.45	7.15
1989	5.7	1.45	7.15
1990	6.2	1.45	7.65

Reasons for change

In conjunction with other changes in the law which are designed to help insure the solvency of the OASDI Trust Funds, the committee has found it necessary to advance the OASDI increase scheduled for 1985 to 1984 and part of the increase scheduled for 1990 to 1988. In order to cushion the impact on workers of the first change, a one-time tax credit is provided to employees equal to the 1984 increase in the employees FICA tax.

Explanation of provision

The bill provides a new schedule of OASDI rates and leaves HI rates unchanged. The new OASDI rates and combined OASDHI rates are as follows:

EMPLOYER-EMPLOYEE RATE (EACH)

Year	OASDI	HI	OASDI-HI
1984	5.70	1.30	7.00
1985	5.70	1.35	7.05
1986	5.70	1.45	7.15

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EMPLOYER-EMPLOYEE RATE (EACH)—Continued

Year	OASDI	HI	OASDI-HI
1987	5.70	1.45	7.15
1988	6.06	1.45	7.51
1989	6.06	1.45	7.51
1990	6.20	1.45	7.65

Because railroad retirement (RR) payroll taxes are linked to the rates for social security, the committee's bill also provides similar increases in the corresponding railroad retirement taxes.

The bill provides emplyees a credit equal to 0.3 percent of compensation subject to the FICA and RR taxes and to payments of amounts equivalent to FICA taxes under section 218 of the Social Security Act. Because the credit is to be taken into account at the time the tax is collected (by deduction from the employees' wages or otherwise), the net OASDI employee tax rate for 1984 will be 5.40 percent. However, employees' annual wage statements are to show the gross FICA tax (7.00 percent of wages) and the credit amount (0.3 percent of wages) separately. As under present law, the appropriation of funds into, for example, the OASDI trust funds will be based on the gross OASDI employee tax rate, which will be 5.70 percent and, thus, will not be affected by the credit.

Effective date.—These provisions will apply to remuneration paid after December 31, 1983.

C. Self-employment income tax and credit (secs. 133 of the bill and secs. 43, 164, 275, 401, 1401, and 1402 of the Code)

Present Law

The Self-Employment Contributions Act (SECA) imposes two taxes (OASDI and HI) on self-employed individuals. Self-employed persons pay an OASDI tax rate that is equal to approximately 75 percent of the combined employer-employee rate and an HI tax rate that is equal to 50 percent of the combined employer-employee rate.

The presently scheduled OASDI rates for self-employment income are as follows:

IN THE CASE OF A TAXABLE YEAR

Beginning after	and before:	percent
December 31, 1981	January 1, 1985	8.05
December 31, 1984	January 1, 1990	8.55
December 31, 1989		9.30

The HI rates for self-employment income are as follows:

IN THE CASE OF A TAXABLE YEAR

Beginning after	and before:	percent
December 31, 1980	January 1, 1985	1.30
December 31, 1984	January 1, 1986	1.35

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IN THE CASE OF A TAXABLE YEAR—Continued

Beginning after:	and before:	percent.
December 31, 1985		1.45

Under present law, the expenses of compensation or purchased services, including wages, the employer FICA tax, and payments to self-employed individuals are deductible, for income tax purposes, as business expenses. However, neither the employee FICA tax nor the SECA tax is deductible.

Reasons for change

The committee is concerned that, under the current system, self-employed individuals pay into the social security system less than employers and employees, taken together, contribute for equal benefits. Thus, even though an employer may take an income tax deduction for his share of the payroll tax paid on behalf of an employee and Federal revenues would be reduced thereby, the social security trust funds received less than is necessary to provide benefits to self-employed individuals. This disparity in receipts contributes to the financial difficulties of the social security system.

Explanation of provisions

Under the bill, the OASDI rate on self-employment income will be equal to the combined employer-employee OASDI rate, and the HI tax rate on self-employment income will be equal to the combined employer-employee HI rate. In order to cushion the impact of the increase, the bill provides a permanent credit against SECA taxes.

The OASDI tax rate on self-employment income will be:

IN THE CASE OF A TAXABLE YEAR

Beginning after:	and before	percent
December 31, 1983	January 1, 1988	11.40
December 31, 1987	January 1, 1990	12.12
December 31, 1989		12.40

The HI rate for self-employed persons will be:

IN THE CASE OF A TAXABLE YEAR

Beginning after:	and before:	percent
December 31, 1983	January 1, 1985	2.60
December 31, 1984	January 1, 1986	2.70
December 31, 1985		2.90

Beginning in 1984, self-employed persons will be entitled to a permanent credit against SECA tax. For 1984, the credit will be 2.9 percent of self-employment income. For 1985, the credit will be 2.5 percent. For 1986, the credit will be 2.2 percent. For 1987–1989, the

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credit will be 2.1 percent. For 1990 and subsequent years, the rate of the credit will be 2.3 percent. The SECA tax credits may be taken directly into account in computing SECA liability for a taxable year and estimated tax payments for that year.

The SECA tax credits will not reduce the revenues of the social security trust funds, since under the Social Security Act, appropriations into the trust funds will be based on the SECA tax rates specified above without regard to the credits allowed against such taxes.

Effective date.—The provisions will be effective for taxable years beginning after December 31, 1983.

REALLOCATION OF OASDI TAX RATE

(Section 141 of the Bill)

Present law

The tax rate allocation between OASI and DI is fixed in the law. The following table displays the allocation for employers, employees and the self-employed:

OASDI TAX RATES

[In percent]

	Employers and employees, each			Self-employed		
	OASI	DI	OASDI	OASI	DI	OASDI
1982 to 1984	4.575	0.825	5.4	6.8125	1.2375	8.05
1985 to 1989	4.750	.950	5.7	7.1250	1.4250	8.55
1990 and later	5.100	1.100	6.2	7.6500	1.6500	9.30

Committee amendment

The Committee amendment would reallocate the OASDI tax so that both trust funds will have about the same reserve ratios (i.e., reserves at the beginning of a year as a percentage of outgo during the year). This is the same as the recommendation of the National Commission on Social Security Reform.

The following table displays the new allocation for the OASDI tax rate:

[In percent]

	Employers and employees, each			Self-employed		
	OASI	DI	OASDI	OASI	DI	OASDI
1983	5.075	0.625	5.7	10.4625	0.9375	11.40
1984 to 1987	5.20	.50	5.7	10.4	1.0	11.40
1988 to 1989	5.53	.53	6.06	11.06	1.06	12.12
1990 to 1999	5.60	.60	6.20	11.2	1.20	12.40
2000 and later	5.55	.65	6.20	11.1	1.30	12.40

Effective.—The first reallocation would apply for 1983.

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INTERFUND BORROWING EXTENSION

(Section 142 of the Bill)

Present law

Public Law 97-123 authorized, through December 31, 1982, borrowing between the OASI, DI, and HI trust funds whenever it was determined by the Managing Trustee (the Secretary of Treasury) that additional funds were needed to pay benefits. The Conference Report specified that amounts borrowed could not exceed what was required to ensure benefit payments through June 1983. Under this authority, and to fulfill this purpose, $17.5 billion was transferred to the OASI trust fund from the DI and HI trust funds in 1982 (of which $12.4 billion was from HI).

Under the law, the borrowing fund is required to make periodic interest payments on outstanding balances. Also the loan must be repaid when the Managing Trustee determines that the assets of the borrowing fund are sufficient to begin repayment.

Committee amendment

Through 1987, the committee amendment would authorize interfund borrowing between the OASI, DI, and HI trust funds. The following protections would be provided for the HI trust fund: (1) interest would be paid monthly to HI on any outstanding loans to OASDI; (2) OASDI could not borrow from HI in any month the HI trust fund ratio is under 10 percent (with no more to be borrowed than would reduce such ratio to 10 percent); (3) in 1983-87, OASDI would repay loans from HI whenever the OASDI fund ratio at the end of the year exceeds 15 percent; and (4) in 1988-89, OASDI would repay HI, in 24 equal monthly payments, the loan balance outstanding at the end of 1987 (plus interest on any outstanding loan balance).

Similar protections would be provided for the OASI and DI trust funds in the event that HI were to borrow from OASDI.

The amendment is similar to the recommendation of the National Commission on Social Security Reform to authorize, through 1987, interfund borrowing between the OASI and DI trust funds and to the OASI and DI trust funds from the HI trust fund.

Under the Committee amendment, using intermediate cost estimates the amounts available from the HI trust fund for loans (in excess of the 10 percent requirement) to the OASDI trust funds would be about $7 billion in 1984, $5 billion in 1985, $4 billion in 1986, and $3 billion in 1987; however, under this estimate the OASDI trust funds would not need any further loans in 1983-87. Under the pessimistic cost estimate, such amounts available from the HI trust fund would be about $6 billion in 1984, $4 billion in 1985, and zero in 1986-87; however, under this estimate the OASDI trust funds would not need any further loans in 1983-87 (although slightly worse experience during that period would make loans necessary).

Effective.—On enactment.

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CREDIT AMOUNTS OF UNNEGOTIATED CHECKS TO THE TRUST FUNDS

(Section 143 of the Bill)

Present law

The social security trust funds are not credited for OASDI benefit checks which remain uncashed. Instead, the value of benefit checks which are not cashed remains in the General Fund of the Treasury.

Committee amendment

The Committee amendment would provide for a lump-sum payment to the OASDI trust funds from the General Fund representing the amount of uncashed benefit checks which have been issued in the past. In addition, it would require the implementation of a procedure under which: (1) the Treasury Department would make it possible to distinguish OASDI checks from other government checks; and (2) the trust funds would be credited on a regular basis with an amount equal to the value of all OASDI benefit checks which have not been negotiated for a period of twelve months. This is similar to the recommendation of the National Commission on Social Security Reform which required only the initial lump sum transfer, assuming that future transfers were already provided for.

Effective date.—The lump sum transfer would be made in the month following the month of enactment of this provision.

OASDI REVENUE GAIN

[In billions, calendar years]

	1983	1984	1985	1986	1987	1988	1989	1983–89
Short range	$0.8	([1])	([1])	([1])	([1])	([1])	([1])	$1.1
Long range: negligible.								

[1] Less than $50 million.

MILITARY WAGE CREDITS

(Sections 144 and 145 of the Bill)

Present law

Since 1946, the OASDI system has provided gratuitous wage credits to persons who serve in the military forces. Such military personnel have been credited with earnings (upon which benefits are based) for which no payroll taxes have been paid. Two types of credits have been given: (1) for World War II veterans, noncontributory wage credits of up to $1,920 per year for active military service from 1940 to 1957; and (2) noncontributory wage credits of $1,200 per year for military service performed after 1956 to recognize the value of non-cash compensation, such as food, shelter and medical services. (In 1957, members of the military were compulsorily covered under social security.)

To finance the costs incurred in paying the benefits based on periods of military service for which no contributions were made, the

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social security trust funds receive reimbursements from the General Fund of the Treasury. The annual reimbursement to the trust funds has been about $700 million in recent years.

Committee amendment

The Committee amendment would credit the OASDHI trust funds, in a lump sum, with an amount equal to the estimated additional cost of providing future benefits based on pre-1957 military wage credits. In addition, the OASDHI trust funds would be credited with a lump sum payment equaling the taxes that would be credited with a lump sum payment equaling the taxes that would have been collected and the interest that would have been earned if the credits for service after 1956 and before 1983 had been taxed as they were earned, less the reimbursements already received. Beginning in 1983, a general fund appropriation would reimburse the trust funds on a current basis for the employer-employee taxes on additional military wage credits given for non-cash compensation.

This is the same as the recommendation of the National Commission on Social Security Reform except that the Committee has extended the provision to include HI.

Effective date.—Lump sum is payable in the month following the month of enactment. Lump sums would be payable within 30 days after the enactment of this provision.

OASDI REVENUE GAIN

[In billions, calendar years]

	1983	1984	1985	1986	1987	1988	1989	1983 89
Short range	$18.4	−$0.4	−$0.4	−$0.3	−$0.4	−$0.4	−$0.4	$16.0
Long range: plus .01 of taxable payroll.								

TRUST FUND INVESTMENT PROCEDURE

(Section 146 of the Bill)

Present law

Payroll tax revenues which are in excess of the amount necessary to pay current benefits must be invested, generally in "special issue" obligations available for purchase only by the trust funds. Such obligations have maturities fixed with "due regard" for the needs of the trust funds and bear an interest rate equal to the average market yield on all marketable, interest bearings obligations of the U.S. government which are not due or callable for at least 4 years.

The maturity dates on new special issues and the redemption schedule for trust fund investments are not set by law, but by Treasury procedure. The Treasury attempts to set the maturity dates for special issues from 1 to 15 years—so that about 1/15 of the total portfolio comes due in each of the next 15 years. When securities must be sold to meet benefit obligations, special issues with the shortest duration until maturity are sold first. In the event that

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there are several securities with the same duration until maturity, those with the lowest interest rate are sold first.

Committee amendment

The Committee amendment provides for reinvesting all trust fund assets each month at a rate of interest based on the average market rate on all public-debt obligations currently held by Treasury with a duration of four or more years until maturity.

The amendment would require the Managing Trustee to: (1) redeem all present special issues at their face amount; (2) redeem all flower bonds (marketable government bonds which, for inheritance tax purposes, are redeemable at par) at their current market values; and (3) invest, on a monthly basis, the redeemed investments and all future funds only in separate depository accounts for each of the trust funds.

This is similar to the recommendation of the National Commission on Social Security Reform, except that the Commission recommended investing in special issues.

Effective.—The first day of the first month beginning more than 30 days after the date of enactment.

Revenue Gain: No significant gain or loss anticipated.

PUBLIC MEMBERS ON BOARD OF TRUSTEES

(Section 147 of the Bill)

Present law

The Board of Trustees of the four social security trust funds (Old-Age and Survivors Insurance, Disability Insurance, Hospital Insurance, and Supplemental Medical Insurance) consists of, ex officio, the Secretaries of the Treasury, Health and Human Services, and Labor, with the Secretary of the Treasury serving as the managing trustee. Among other responsibilities, the Board of Trustees is required to report to Congress each year on the operation and status of the trust funds, review the general policies followed in managing the trust funds, and recommend changes in such policies.

Committee amendment

The Committee amendment would add two public members to the Board to Trustees of the OASDI, HI, and SMI trust funds. The public members would be nominated by the President and confirmed by the Senate. The two public members could not be from the same political party. Public members would not be considered fiduciaries and would not be personally liable for actions taken in such capacity with respect to the trust funds.

The National Commission on Social Security Reform also proposed that the Board of Trustees of the OASDI trust funds be expanded to include two public members.

Effective.—On enactment.

Cost.—None.

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ACCELERATE STATE AND LOCAL DEPOSITS

(Section 148 of the Bill)

Present law

Requires the deposit of withheld social security taxes for State and local employees within thirty days after the end of the month in which the applicable wages were paid.

By contrast, the frequency with which deposits of social security taxes and income taxes are made by private employers is determined under regulations issued by Treasury and vary in accordance with the tax liability of the employer. Deposits are required as frequently as every week for employers with large liabilities and as infrequently as every three months for employers with smaller liabilities.

Although State and local governments are now governed by the same rules as private employers with regard to depositing withheld income taxes, deposits of social security taxes continue to be treated differently.

Committee amendment

The Committee amendment would apply the same social security tax deposit requirements to State and local governments that now apply to private employers.

Effective date.—Effective for deposits required to be made after December 1983.

OASDI REVENUES

[In billions, calendar years]

	1984	1985	1986	1987	1988	1989	1983–89
Short range	$1.4	$0.1	$0.1	$0.1	$0.3	$0.2	$2.2
Long-range: Negligible.							

TRIGGERED NORMALIZATION OF TAX TRANSFERS

(Section 149 of the Bill)

Present law

Under current procedures, social security taxes are transferrred to the trust funds on a daily basis on Treasury estimates of amounts collected. OASDI benefit payments, however, are concentrated at the start of the month creating the need for high balances in the OASDI trust funds during the first week of the month.

Committee amendment

The Committee amendment provides that, when at the start of any month, the Secretary of Treasury determines that the reserves of the OASDI trust funds are inadequate to meet 1½ months of benefits (reserves less than 12% of outgo), the Secretary would be required to credit the trust funds on the first day of the next month with the full payroll tax revenues estimated for the month.

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Interest would be paid to the General Treasury on the excess sums so transferred at a rate equal to the average 91-day Treasury bill rate during the month, with such interest being payable at the end of each month.

Effective.—On enactment through 1987 (when the authority for interfund borrowing expires).

Cost.—Negligible.

Treatment of certain deferred compensation and salary reduction arrangements (sec. 150 of the bill and sec. 3121(a) of the Code).

Present law

Cash or deferred arrangements

Under a qualified cash or deferred arrangement (sec. 401(k)) forming a part of a tax-qualified profit-sharing or stock bonus plan, a covered employee may elect to have the employer contribute an amount to the plan on the employee's behalf or to receive such amount directly from the employer in cash. Amounts contributed to the plan pursuant to the employee's election are treated as employer contributions to the plan and are excluded from the employee's taxable income and social security wage base.

Amounts distributed with respect to an employee under a qualified plan generally are includible in the recipient's income, but are excluded from the social security wage base.

Tax-sheltered annuities

Under present law, tax-sheltered annuities (sec. 403(b)) may be purchased on an individual basis for employees of public schools or tax-exempt religious, charitable, and other organizations described in section 501(c)(3). Subject to certain limitations, amounts paid by the employer to purchase the annuity are excluded from the employee's income. A tax-sheltered annuity may be purchased for an employee pursuant to a salary reduction agreement between the employer and the employee.

The Internal Revenue Service has ruled that amounts paid for a tax-sheltered annuity pursuant to a salary reduction agreement are includible in the employee's social security wage base, even though such amounts may not be subject to income tax withholding. The validity of the ruling position is in doubt in light of the Supreme Court decision in *Rowan Companies, Inc.* v. *United States* (see following section of this report).

Amounts distributed under a tax-sheltered annuity generally are includible in the recipient's income, but are excluded from the social security wage base.

Cafeteria plans

Under an employer's cafeteria plan (sec. 125), a covered employee may choose among various benefits, which may include cash, taxable benefits, or nontaxable benefits. If certain requirements are met, amounts applied under a cafeteria plan toward nontaxable benefits (*e.g.,* accident and health benefits or plan contributions under a qualified cash or deferred arrangement) are excluded from the employee's income and generally from the social security wage

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base. Taxable benefits chosen by the employee (*e.g.,* cash) are includible in income and generally includible in the wage base.

Eligible State deferred compensation plans

Under an eligible State deferred compensation plan (sec. 457(a)), an employee of a State or local government or a rural electric cooperative may elect to defer compensation, subject to certain limits. Amounts deferred under an eligible plan are excluded from income until paid to the employee under the plan. Eligible State deferred compensation plans generally are not retirement plans for purposes of the rules defining "wages" includible in the social security wage base. (For example, the income tax rules for eligible plans permit distributions to an employee after age 59½ without regard to whether the employee is retired.) Thus, amounts deferred are includible in the social security wage base at the time of the deferral if the plan is not a retirement plan.

Non-qualified deferred compensation plans

Under present law (sec. 3121(a)), standby pay or payments made to an employee on account of retirement, either on an individual basis or under a plan or system of the employer providing for employees generally, may be excluded from the social security wage base without regard to whether the payments are under a tax-qualified retirement plan (sec. 401(a) or 403(a)) or other tax-favored retirement savings program (e.g., a tax-sheltered annuity (sec. 403(b)).

Reasons for change

Generally, if an employee receives cash and then chooses to use these funds for personal savings or benefits, the amount of cash received is subject to FICA. This is true, for example, for contributions to an individual retirement account (IRA) even if the employer transmits the funds directly to the IRA account.

Under cash or deferred arrangements, certain tax-sheltered annuities, certain cafeteria plans, and eligible State deferred compensation plans, the employer contributes funds which are set aside by individual employees for individual savings arrangements, and thus, the committee believes that such employer contributions should be included in the FICA base, as is the case for IRA contributions. Otherwise, individuals could, in effect, control which portion of their compensation was to be included in the social security wage base. This would make the system partially elective and would undermine the FICA tax base.

The committee also believes that it is appropriate to exclude payments from the social security wage base where the payments are made from a tax-qualified or other tax-favored retirement plan. However, the committee does not believe that such tax-favored treatment under the FICA tax rules generally should be extended to deferred compensation plans which do not qualify for tax-favored treatment under the income tax rules.

Explanation of provision

Under the bill, an employer's plan contributions on behalf of an employee under a qualified cash or deferred arrangement will be

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includible in the social security wage base for tax and coverage purposes to the extent that the employee could have elected to receive cash in lieu of the contribution. The provision is intended to apply to elective amounts under the cash or deferred arrangement and not to nonelective amounts contributed by employers to a qualified profit-sharing or stock bonus plan of which the arrangement may be a part.

The bill also provides that any amounts paid by an employer to a tax-sheltered annuity by reason of a salary reduction agreement between the employer and the employee would be includible in the employee's social security wage base. The committee intended that the provision would merely codify the holding of Revenue Ruling 65-208, 1965-2 Cum. Bull. 383, without any implication with respect to the issue of whether a particular amount paid by an employer to a tax-sheltered annuity is, in fact, made by reason of a "salary reduction agreement".

In addition, amounts subject to an employee's designation under a cafeteria plan that includes a qualified cash or deferred arrangement will be includible in the social security wage base to the extent that such amounts may be paid to the employee in cash or property or applied to provide a benefit for the employee that is not otherwise excluded from the definition of wages under section 3121 of the Code.

The bill would also include in the social security wage base amounts deferred under an eligible State deferred compensation plan (sec. 457(a)). The payment to such a plan would be treated as wages received in the year in which the services relating to the payment were performed. However, no change is made to the present-law self-employment tax (SECA) rules regarding amounts paid under an eligible State deferred compensation plan on behalf of an independent contractor.

Under the bill, nonqualified deferred compensation generally is includible in the social security wage base when it becomes available to the employee. For this purpose, nonqualified deferred compensation generally includes payments under a deferred compensation arrangement which is not (1) a tax-qualified plan, (2) an individual retirement arrangement (IRA), (3) a simplified employee pension (SEP), (4) a tax-sheltered annuity, or (5) a governmental plan. A governmental plan is one established and maintained for its employees by the Government of the United States, by any State or political subdivision thereof, or by any agency or instrumentality of any of the foregoing. However, elective deferrals under an eligible State deferred compensation plan (sec. 457(a)) are includible in the wage base as described in the preceding paragraph, and amounts payable under a deferred compensation plan of a State or local government which is not an eligible plan (sec. 457(e)(1) and (e)(2) (D) and (E)) are includible in the wage base when there is no substantial risk of forfeiture by the employee.

The bill also includes conforming changes to the provisions (sec. 3306) defining "wages" for purposes of the Federal Unemployment Tax Act (FUTA). Deferred compensaiton includible in the social security wage base under the bill would also be treated as wages for FUTA purposes. In addition, the bill provides that certain sick pay which is includible in the social security wage base under provi-

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sions enacted in 1978 would also be treated as wages for FUTA purposes.

Effective date.—These changes apply to remuneration paid after December 31, 1983. Codification of Rowan decision with respect to meals and lodging (sec. 151 of the bill and sec. 3121(a) of the Code).

Present law

Under present law, amounts which constitute wages for income tax withholding purposes (Code sec. 3401) and amounts which constitute wages for social security tax purposes (Code sec. 3121) are separately defined. However, in *Rowan Companies, Inc. v. United States,* 452 U.S. 247 (1981), the Supreme Court held that the definition of wages for social security tax purposes and the definition of wages for income tax withholding purposes must be interpreted in regulations in the same manner in the absence of statutory provisions to the contrary.

At issue in *Rowan* was whether the value of meals and lodging provided employees at the convenience of the employer were wages for social security tax purposes (*i.e.,* were includable in the social security wage base). The value of such employer-provided meals and lodging may be excluded from the income of an employee (sec. 119). Treasury regulations required that the value of the meals and lodging be included in the social security wage base, but excluded such value from the definition of wages subject to income tax withholding. The Supreme Court decision invalidated those Treasury regulations which required that the value of the meals and lodging be included in the social security wage base.

Reasons for change

The social security program aims to replace the income of beneficiaries when that income is reduced on account of retirement and disability. Thus, the amount of "wages" is the measure used both to define income which should be replaced and to compute FICA tax liability. Since the security system has objectives which are significantly different from the objective underlying the income tax withholding rules, the committee believes that amounts exempt from income tax withholding should not be exempt from FICA unless Congress provides an explicit FICA tax exclusion.

Explanation of provision

The bill provides that, with the exception of the value of meals and lodging provided for the convenience of the employer, the determination whether or not amounts are includible in the social security wage base is to be made without regard to whether such amounts are treated as wages for income tax withholding purposes. Accordingly, an employee's "wages" for social security tax purposes may be different from the employee's "wages" for income tax withholding purposes. In addition, the bill provides that the definition of wages for social security tax and benefit purposes is revised to exclude the value of employer-provided meals and lodging to the extent such value is also excluded from the employee's gross income.

Effective date.—The provision applies to remuneration paid after December 31, 1983.

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Treatment of contributions under simplified employee pensions (SEPs) (sec. 152 of the bill and sec. 3121(a)(5) of the Code)

Present law

Under present law, the Internal Revenue Code excludes from the social security wage base employer payments to or on behalf of an employee under a simplified employee pension (SEP). However, such employer contributions are treated as covered wages for social security benefit purposes.

Reasons for Change

The committee believes that is is inappropriate to treat employer payments to a SEP as covered wages for benefit purposes where such amounts are excluded from the social security wage base for tax purposes.

Explanation of provision

The bill amends the Social Security Act to exclude from the definition of covered wages for social security coverage purposes employer contributions to a SEP that are deductible as such by the employer. The bill makes clear that the exclusion applies, for both tax and coverage purposes, only with respect to the employer's contribution to a SEP, not with respect to the amount equivalent to the employee's contribution to an individual retirement arrangement (IRA).

Effective date.—This provision applies to remuneration paid after December 31, 1983.

ESTIMATED REVENUE EFFECTS OF CERTAIN COMMITTEE PROVISIONS [1]

[In millions of dollars]

Provision and receipts or liabilities	Calendar or fiscal year—						Total
	1984	1985	1986	1987	1988	1989	
Taxation of OASDI benefits: [2]							
Calendar year [3]	2,637	3,181	3,847	4,603	5,500	6,544	26,312
Fiscal year	848	2,805	3,387	4,079	4,878	5,818	21,815
Taxation of tier I railroad retirement benefits:							
Calendar year [4]	61	71	81	94	108	124	538
Fiscal year	20	64	74	85	98	113	453
Tax credit for 1984 FICA taxes: [2]							
Calendar year	4,434						4,434
Fiscal year	3,234	1,200					4,434
SECA provisions: [2]							
Increase in OASDI and HI rates for SECA:							
Calendar year	4,490	4,361	4,744	4,973	6,133	6,476	31,177
Fiscal year	1,497	4,447	4,489	4,820	5,360	6,247	26,860
SECA credit:							
Calendar year	−2,800	−2,596	−2,427	−2,428	−2,565	−2,709	−15,525
Fiscal year	−933	−2,732	−2,540	−2,427	−2,474	−2,613	−13,719
Net effect:							
Calendar year	1,690	1,765	2,317	2,545	3,568	3,767	15,652
Fiscal year	564	1,715	1,949	2,393	2,886	3,634	13,141

[1] In addition to the provisions shown, the committee estimates that the provisions regarding the inclusion in the FICA wage base of amounts received under certain deferred compensation and salary reduction agreements will increase receipts of the social security trust funds by $2.0 billion during calendar years 1984 to 1989, inclusive.

[2] These estimates are consistent with the II-B assumptions used by the Social Security Administration in preparing the Trust Fund estimates shown elsewhere in this report.

[3] These amounts are estimated to be transferred to the Social Security Trust Funds during the calendar year shown.

[4] These amounts are estimated to be transferred to the Railroad Retirement Account during the calendar year shown.

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TITLE II OF THE BILL

Increase the SSI Payment Standard and Modify Pass-Through Requirements

(Sections 201 and 202 of the Bill)

Present law

The first $20 of income received by an individual in a month is disregarded in determining SSI eligiblity and benefit amount. The income may be earned or unearned (except for some income based on need, such as veterans' pensions, which is fully counted). The disregard was provided in the original statute in 1972 to ensure that persons who had contributed toward an entitlement, such as OASDI, were better off than those who had not. The amount of the disregard has not been increased since 1972.

Committee amendment

The Committee amendments would:

A. Increase the SSI payment standard applicable to all individuals by $20 ($30.00 for a couple) per month, effective July 1983; and

B. To help protect the States from increased costs resulting from this provision, expand current law to allow States to meet the "pass through" requirement for 1983 if they pass through the equivalent of the COLA that would have occurred under current law rather than the proposed monthly payment increase. Presently, States which provide payments to supplement the Federal SSI payment are required to pass through to recipients any Federal SSI cost-of-living increases. States have two basic options for meeting the pass through requirements: 1) they may maintain the supplementary payment levels that were in effect for categories of individual recipients in December 1976, or 2) they may make State supplementary payments in any current 12-month period that are no less, in the aggregate, than were made in the previous 12-month period.

The National Commission on Social Security Reform recommended that, effective July 1983, the SSI disregard be increased by $30 per month for OASDI income (not other income) in determining an individual's SSI eligibility and benefit amount. The effect would have been to increase by $30 the monthly income of those individuals who are entitled to both OASDI and SSI.

Presently, the maximum Federal SSI payment is $284 monthly for an individual and $426 monthly for a couple. After certain disregards, the amount of SSI actually received by an individual is reduced on account of other income.

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SSI COST (BASED ON CBO ESTIMATES)

[In millions, fiscal years]

	1983	1984	1985	1986	1987	1988
$20 payment standard increase	$250	$750	$845	$840	$875	$935

SSI Alert

(Section 203 of the Bill)

Present law

Currently, there is no statutory requirement that OASDI beneficiaries be contacted and informed of potential eligibliltiy for Supplemental Security Income (SSI) payments. However, since the begnning of the SSI program, the Social Security Administration has undertaken a number of outreach efforts to identify those potentially eligible. SSA routinely provides information about 581 eligibility and takes applications for SSI payments at the time of application for OASDI benefits if the applicant is potentially eligible for SSI payments. In addition, many State agencies and other private relief groups routinely refer clients to SSA. Presently, about 6.9 percent of elderly social security recipients also receive SSI.

Committee amendment

The Committee amendment would require the Secretary of Health and Human Services to notify, on a one-time basis, all elderly OASDI beneficiaries who are potentially eligible of the availability of SSI and encourage them to contact their district offices. In addition, the provision would require that the same information be included with the notification to OASDI beneficiaries of upcoming eligibility for Supplemental Medical Insurance.

Despite the current and past activities of the Social Security Administration to make persons potentially eligible for SSI aware of the existence of the program, the Committee believes that there may be currently needy OASDI beneficiaries who have been on the social security rolls for a period of time who may have applied for social security prior to the availability of SSI or who may not have been eligible at the time they applied but whose circumstances have since changed.

The Committee provision would alert those OASDI beneficiaries to the availability of the SSI program and would, in the future, also provide notification to those approaching the age of eligibility (age 65) through information contained with a notice of future eligibility for Supplemental Medical Insurance which is mailed approximately three months before a beneficiary attains age 65.

Effective date.—Notification to those on the rolls must be made before July 1, 1984.

Cost.—Unable to estimate.

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TITLE III OF THE BILL

Description of Medicare Prospective Payment Provision

GENERAL SUMMARY

Present law

Under current law, medicare reimburses hospitals on the basis of the "reasonable costs" they incur in providing covered services to beneficiaries, excluding any part of such costs found to be unnecessary in the efficient delivery of needed services. The Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) expanded and added to existing medicare limits on reasonable cost reimbursement for hospitals by (1) expanding the existing "section 223" reimbursement limits to apply to total inpatient operating costs (not just routine costs) and (2) adding temporary growth rate limits (expiring after fiscal year 1985) which would rise annually by one percentage point plus the increase in the "market basket" of goods and services purchased by hosptials. TEFRA also directed the Secretary of the Department of Health and Human Services (HHS) to develop and report to Congress proposals for the reimbursement of hospitals under medicare on a prospective basis. The Department's report was submitted in late 1982, and its recommendations have been embodied in Administration-sponsored legislation. The Committee amendment is a modified version of the Administration's proposal.

Committee amendment

The committee amendment includes a major change in the method of payment under medicare for inpatient hospital services. Medicare payment for inpatient operating costs of hospitals would be determined in advance and paid on a per case basis. A fixed amount would be paid for each type of case, identified by the "diagnosis related group" (DRG) into which the case is classified. These changes are intended to create incentives for hospitals to operate in a more efficient manner, since hospitals would be allowed to keep payment amounts in excess of their costs and would be required to absorb any costs in excess of the DRG rates. Hospitals would be prohibited from charging medicare beneficiaries any amounts in excess of the deductibles and coinsurance provided for by law.

The committee amendment would be effective for individual hospital cost reporting periods beginning on or after October 1, 1983, and would be phased-in over a 3-year period.

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1. Prospective payment amounts

Present law

Under current law, medicare payments for inpatient hospital services are retrospectively-determined based upon a hospital's reasonable costs, subject to certain limits. These reimbursement limits include (1) limits on a hospital's inpatient operating costs (the "section 223" limits) and (2) rate of increase limits on overall inpatient operating costs (a limit which expires after fiscal year 1985).

Committee amendment

(a) Diagnosis-related groups (DRG's).—Under the committee's amendment, the Secretary would be required to determine prospectively a payment amount for each medicare hospital discharge. Discharges would be classified into diagnosis related groups (DRG's) which classify patients into groups that are clinically coherent and relatively homogenous with respect to resource use. The DRG classification system, developed some years ago, has been improved in recent years and represents the most fully developed case classification system representative of a national data base and readily adaptable to a national program. The committee recognizes that in developing a separate payment rate for each DRG it will be necessary to rely on currently available data sources and to use a sample of cases, e.g., the 20 percent sample of medicare beneficiary bills (MEDPAR), to arrive at the DRG rates. The committee expects that the Secretary will refine the DRG rates as better data become available.

The committee recognizes that there may be insufficient data with which to calculate relative prices for some DRG's Because of the small number of medicare cases in some diagnosis related groups. While this has not been a major problem in the past in the design of a case-mix adjustment using DRGs (in connection with the section 223 reimbursement limit under current law), it is important in the prospective payment system to establish a rate for every DRG whether or not it is likely that a case will actually occur. Therefore, the committee recognizes that the Secretary will need to rely on an alternative method for setting the prospective rate for low-volume DRG's—for example, by combining MEDPAR data for several years or by reference to an external source in which these DRG's are more common, e.g., data from State systems.

(b) DRG payment rates.—Under the committee's amendment the Secretary would be required to determine a national standard payment rate per discharge for each DRG. The rate would be the product of:

(1) the average of the standardized cost per discharge, for all hospitals in the country, as determined by the Secretary; and

(2) a weighting factor for each DRG, as determined by the Secretary.

In addition, DRG payment rates would be established for urban and rural areas both nationally and in each of four census regions of the country (the 50 States and the District of Columbia) in order to moderate the impact of the prospective payment system for urban and rural hospitals in different regions of the country. Using

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data from the Bureau of Labor Statistics, each of these payment rates would be adjusted for area differences in hospital wage levels, in similar fashion to the wage adjustment currently used under the section 223 hospital limits.

Hospitals or units of hospitals which are exempted from the prospective payment system would be subject to the rate of increase limits applicable under present law. The current section 223 limits would no longer apply to any of the facilities not included in the prospective payment system for any cost reporting periods beginning on or after October 1, 1983.

(c) Establishment of initial payment rates.—The process for determining DRG payment rates for the first year of the program (fiscal year 1984) begins with the determination of allowable operating costs for inpatient hospital services for each hospital for the most recent cost reporting period for which data are available. These cost data would be updated for fiscal year 1983 by the estimated industry-wide actual increase in hospital costs and further updated for fiscal year 1984 by the hospital market basket increase, plus one percentage point. The resulting amounts would be standardized by excluding an estimate of indirect medical education costs, adjusting for area wage variations, and adjusting for variations in case mix. The Secretary would then compute an average of these standardized cost levels per discharge for the urban hospitals (as currently defined for purposes of the "section 223" limits) in each of the four census regions and nationally and also for the rural hospitals in each of the census regions and nationally.

Each of the average standardized amounts would be reduced to account for payment that will subsequently be made (see below) to specific hospitals for atypical cases ("outliers").

These average standardized amounts would then be reduced as may be required, to achieve budget neutrality in relationship to the reimbursement provisions that would have applied under the 1982 TEFRA legislation. In determining budget neutrality for the DRG part of the payment, the Secretary would include in the DRG payment amounts the additional payments for outlier cases, for indirect medical education costs, and for costs of nonphysician services to inpatients previously paid for under part B, and additional payments reflecting other adjustments.

The Secretary would next determine a separate urban and rural DRG-specified rates for each census region and the nation by computing the product of the average standardized amounts described above and the weighting factor for each DRG (reflecting the relative use of hospital resources for specific DRG's compared for resources used for other DRG's).

The DRG-specific rates would be further adjusted to recognize area wage differences both nationally and on a regional basis for purposes of determining the payment amount using methodologies similar to those currently used under the section 223 limits. The actual amount of revenue paid to a hospital, in addition to the DRG-specific payment rate, will be, of course, influenced by such factors as: payment for capital costs and costs of approved educational programs on a reasonable cost basis; adjustments for indirect teaching costs; additional payments for atypical—or outlier—cases; and various other exceptions and adjustments.

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Under current law, services provided to medicare beneficiaries who are inpatients of a hospital are generally billed under part A of the medicare program. However, under certain circumstances, payments are made for non-physician services (for example, radiology, laboratory, physical therapy, prosthetics, etc.) which are separately billed by the supplier as a part B service even though they are provided to a hospital inpatient. Thus, under current law, some non-physician services may be billed under part A in one hospital and yet, in another hospital may be billed under part B of the program. However, under the committee's amendment, the prospective payment is intended to be payment in full for all covered items and non-physician services to hospital inpatients. Thus, the current practice of allowing independent practitioners to bill part B for items and services provided to inpatients would no longer be permitted under the prospective payment system. Some hospitals and independent practitioners will have to modify their arrangements.

The committee amendment provides that, effective October 1, 1983, all non-physician services provided to hospital inpatients would be paid only as inpatient hospital services under part A with the adjustments described below.

Because there are some limited situations where particular hospitals have extensively followed the practice of allowing direct billing of part B, modifications of these financial arrangements could threaten the financial stability of some institutions. Under the committee amendment, the Secretary would be granted authority to waive the general rules for these few cases for a limited time period not to exceed the transition period during which the new system is phased in. Upon approval of a hospital's request, the Secretary could allow continued payment of part B billings as long as he subsequently deducted the total payments made for these billings from the payments made under the prospective system to the hospital. If such a waiver is granted, at the end of the transition, the Secretary may provide for such methods of payment under Part A, as is appropriate given the organizational structure of the institution.

The Secretary would be required to provide for publication in the Federal Register, on or before September 1 of each fiscal year (beginning with fiscal year 1983) interim final rates, a description of the methodology and data used in computing the DRG payment rates, any adjustment required to produce budget neutrality in relation to the TEFRA level of medicare reimbursement outlays.

In setting the initial payment rates, the Secretary would also be required to recognize the higher payroll costs some hospitals will incur as the result of being required to enter the social security system, by adjusting base costs for individual hospitals and for the prospective rates to accommodate these additional costs.

(d) Annual Updates of the DRG Payment Rates. For fiscal year 1985, the initial DRG payment amounts would be increased by the marketbasket plus one percentage point. As for fiscal year 1984, reductions would be made in the payment rates for additional costs such as outlier payments, indirect medical education costs, and other adjustments in order to achieve budget neutrality in relationship to the reimbursement provisions which would have applied under the TEFRA reimbursement legislation.

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An independent commission of fifteen experts selected by the Office of Technology Assessment would make recommendations to the Secretary and to Congress prior to April 1, 1985 and each subsequent year on the appropriate percentage increase applicable for the next fiscal year. The Commission would be composed of experts in the provision and financing of health care including physicians, registered professional nurses, employers, insurers, researchers and others. In making its recommendations, the commission would take into consideration changes in the marketbasket, changes in hospital productivity, technological and scientific advances, quality of care (including the quality and skill level of professional nursing required to mantain quality care), and the utilization of relatively costly, though effective, methods of care. The Secretary, taking into account the recommendations of the commission, would determine for each fiscal year beginning for fiscal year 1986, the percentage increase which would be used to update the DRG payment rates.

(e) Recalibration of the DRG's.—The Committee amendment requires the Secretary to adjust the DRG classifications (for grouping hospital discharges) and the DRG weighting factors (which reflect the relative amount of hospital resources used by discharges in a DRG compared to the discharges in other DRG's) at least every five years to reflect changes in treatment patterns, technology, and other factors which may change the relative use of hospital resources.

The Commission (described in d above) would consult with and make recommendations to the Secretary with respect to the DRG recalibrations, based on its own evaluation of scientific evidence with respect to new practices, including the use of new technologies and treatment modalities. The commission will report to the Congress on its evaluation of the Secretary's adjustments to the DRG's.

(f) Atypical cases or "outliers".—The committee recognizes that under a prospective payment system, there will be cases within each diagnostic category (DRG) that will be extraordinarily costly to treat, relative to other cases within the DRG, because of severity of illness or complicating conditions, and are not adequately compensated for under the DRG payment methodology. The committee amendment, therefore, requires the Secretary to provide additional payments for cases which are extraordinarily costly to treat, relative to other cases within the DRG.

Additional payments would be made for discharges that exceed the mean length of stay by some fixed number of days, or by a certain number of standard deviations, whichever is less; and

The Secretary will permit hospitals to appeal for additional payment for cases in which charges adjusted to costs are equal to or exceed some multiple of the DRG rate or some dollar criterion, whichever is greater.

The additional amounts to be paid for day outliers will be a percentage of the standard per diem rate for each day beyond the length of stay cut-off defined above. For cost outliers, additional payments will be paid as a percentage of charges adjusted to costs.

Total expected payments resulting from this policy will be not less than 5 percent, nor more than 6 percent, of total medicare payments to hospitals for inpatient care, and the standard payment rates per case will be reduced to compensate for these outlays.

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2. Exclusion of capital-related expenses and medical education

Present law

Under current law, medicare reimburses hospitals for the reasonable costs of capital (including depreciation, interest and rent). In addition, proprietary hospitals receive a return on net equity. The Secretary is authorized to exclude from reimbursement to providers certain costs related to capital expenditures that have been disapproved through the health planning process.

Medicare reimburses direct medical education expenses, such as the salaries of interns and residents, in approved education programs, on the basis of reasonable cost. The section 223 limits provide an adjustment to recognize individual hospital differences in indirect medical education costs due to approved teaching activities. This adjustment is based on the hospital's ratio of interns and residents to its bed size.

Committee amendment

The committee amendment specifically excludes capital from the prospective payment system until October 1, 1986; such costs would be paid on a reasonable cost basis until the specified date. (See Item 9 below for a description of a study related to capital costs.)

The committee amendment also specifically excludes direct medical education costs from the prospective payment system; such costs would be paid on the basis of reasonable costs.

With respect to indirect medical education costs, an adjustment to a hospital's DRG rates would be allowed equal to twice the adjustment used in connection with the section 223 limits for such costs. This adjustment is provided in the light of doubts (explicitly acknowledged by the Secretary in his recent report to the Congress on prospective payment) about the ability of the DRG case classification system to account fully for factors such as severity of illness of patients requiring the specialized services and treatment programs provided by teaching institutions and the additional costs associated with the teaching of residents. The latter costs are understood to include the additional tests and procedures ordered by residents as well as the extra demands placed on other staff as they participate in the education process.

The committee emphasizes its views that these indirect teaching expenses are not to be subjected to the same standards of "efficiency" implied under the DRG prospective system, but rather than they are legitimate expenses involved in the postgraduate medical education of physicians which the medicare program has historically recognized as worthy of support under the reimbursement system.

The adjustment for indirect medical education costs is only a proxy to account for a number of factors which may legitimately increase costs in teaching institutions. The committee believes that it is important, in addition, to recognize explicitly extraordinary expenses in individual cases, and has therefore required (as discussed elsewhere) an expansion and modification of the Administration's recommended policy regarding atypical cases or outliers

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(which it is reasonable to expect would occur more commonly in teaching hospitals than in other hospitals).

3. Effective date/transition

Present law

Under current law, the section 223 limits are authorized indefinitely; the rate of increase limits do not apply to hospital cost reporting periods beginning on or after October 1, 1985.

Committee amendment

The prospective payment system would be effective for individual hospital accounting years beginning on or after October 1, 1983, and would be phased-in over a three year period. In year one, 25 percent of the payment would be based on a combination of national and regional DRG rates (25 percent national, 75 percent regional); 75 percent would be based on each hospital's own cost-based experience. In year two, 50 percent of the payment would be based on a combination of national and regional DRG rates (50 percent each); 50 percent would be based on each hospital's cost experience. In year three, 75 percent of the payment would be based on a combination of DRG rates (75 percent national, 25 percent regional); 25 percent would be based on each hospital's cost experience. In year four, the entire payment would be based on national DRG rates, calculated separately for hospitals located in urban and rural areas. The phase-in of national DRG rates over the three-year period is designed to minimize disruption that might otherwise occur because of sudden changes in reimbursement levels.

The section 223 limits provided under current law would be repealed effective for hospital cost reporting periods beginning on or after October 1, 1983. However, hospitals or units of hospitals not included in the prospective payment system would be subject to the same rate of increase limitation as contained in TEFRA, including the penalties and bonuses. The rate of increase used to update these limits would be that which is currently contained in TEFRA, market basket plus one percentage point.

4. Exemptions, exceptions and adjustments

Present law

Under current law, section 223 limits do not apply to children's hospitals, psychiatric hospitals, long-term care hospitals or to rural hospitals with less than 50 beds. In addition, the Secretary is required to provide exemptions, exceptions and adjustments to the limits as he deems appropriate to take into account the special needs of psychiatric, public and other hospitals that serve a disproportionate number of low-income and medicare beneficiaries and sole community providers. Current law also requires the Secretary to provide exemptions, exceptions and adjustments to the section 223 limits as he deems appropriate to take into account the special needs of new hospitals, risk-based health maintenance organizations, and hospitals providing atypical or essential services; extraordinary circumstances beyond a hospital's control; and for other purposes.

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Committee amendment

Under the committee amendment, psychiatric, long-term care, rehabilitation and children's hospitals would be specifically exempted from the prospective payment system. The DRG classification system was developed for short-term acute care general hospitals and, as currently constructed, does not adequately take into account special circumstances of diagnoses requiring long stays and as used in the medicare program is inappropriate for certain classes of patients. In addition, distinct part rehabilitation or psychiatric units of acute care hospitals would be exempt. The Secretary, under current medicare rules and regulations, has prescribed in detail standards and criteria that distinct parts must meet including establishment of separate cost entities for cost reimbursement and requirements that such units have a sub-provider identification number.

The Secretary would be required to provide for exceptions and adjustments to take into account the special circumstances faced by sole community providers. Such providers will be paid on the same basis as all other providers are paid in year one: 25 percent of the payment would be based on a blend of rural national and regional DRG rates (25 percent national, 75 percent regional); 75 percent would be based on each hospital's own cost experience. In no case would total payments in any one transition year be less than the payments made in the preceding year.

The committee is concerned that, in determining which hospitals have been eligible for exceptions and adjustments as sole community providers in the past, the Secretary has applied different criteria in the different regions of the country, including some which are very narrow and restrictive. Therefore, the committee expects that the Secretary, in making such determinations for sole community providers under the new prospective payment system, will develop and take into account a much broader range of factors relating to beneficiary access to basic hospital services. The committee amendment further directs the Secretary to study the problems of paying sole community providers and report back to the Congress, by April 1, 1985, on equitable methods of paying these small rural hospitals which take account of their unique circumstances, including their vulnerability to substantial variations in occupancy rates.

Under this amendment, the Secretary would also be required to provide exceptions and adjustments, as he deems appropriate, to take into account the special needs of public or other hospitals that serve a disproportionately large number of low-income and part A medicare beneficiaries. Concern has been expressed that public hospitals and other hospitals that serve such patients may be more severely ill than average and that the DRG payment system may not adequately take into account such factors. The Secretary in his report to Congress stated that the Department of Health and Human Services would continue to study ways of taking account of severity of illness in the DRG system.

Exceptions and adjustments would also be permitted to take into account the special needs of hospitals located in Alaska and Hawaii, as the Secretary now does in applying the reimbursement limits of present law.

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This provision would exempt from the prospective payment system hospitals located in geographic areas outside the fifty States and the District of Columbia but within the United States for purposes of medicare (i.e. territories). The cost experience of these hospitals may be so varied that the DRG prospective payment system may not adequately reflect the needs of these hospitals.

5. Peer review

Present law

Under current law the Secretary is required to enter into contracts for utilization and quality control peer review with professional review organizations or other review organizations, including medicare intermediaries (subject to certain conditions and limitations).

Committee amendment

The committee amendment would require hospitals to contract with a professional review organization (PRO) selected by the Secretary to serve that area, under title XI of the Social Security Act for the review of admissions, discharges and quality of care. The purpose of this contract is to provide for the review of the accuracy of the diagnostic information on the hospital's bills, the completeness and adequacy of the care provided, the appropriateness of its medicare admissions, and the appropriateness of the care provided to patients designated by the hospitals as outliers. These reviews would be covered as a hospital cost of care under Part A, but the PRO would be paid by the Secretary on behalf of the hospital on the basis of a budget approved by the Secretary.

6. Payments to health maintenance organizations (HMO's) and competitive medical plans (CMP's)

Present law

Under current law, health maintenance organizations (HMO's) and competitive medical plans (CMP's) may be reimbursed either on the basis of reasonable costs or under a risk-based contract, a payment equal to 95 percent of the adjusted average per capital cost (AAPCC) for medicare enrollees in the HMO's area.

Committee amendment

Under the committee amendment, an HMO or a CMP that receives medicare payments on a risk-basis may choose to have the Secretary directly pay hospitals for inpatient hospital services furnished to medicare enrollees of the HMO or CMP. The payment amount would be at the DRG rate and would be deducted from medicare payments to the HMO or CMP. The HMO or CMP may alternatively choose to continue to pay the hospital directly.

7. State cost control programs

Present law

Under current law, the Secretary has authority to establish medicare demonstration projects. There are currently four Statewide medicare demonstrations (Maryland, Massachusetts, New

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Jersey, New York) and one area-wide demonstration (Rochester, New York).

In addition, the Secretary is authorized, at the request of a State, to pay for medicare services according to the State's hospital cost control system if such system—

(1) applies to substantially all non-Federal acute care hospitals in the State;

(2) applies to at least 75 percent of all inpatient revenues or expenses in the State;

(3) provides assurances that payors, hospital employees and patients are treated equitably; and

(4) provides assurances that the State's system will not result in greater medicare expenditures over a three-year period than would otherwise have been made.

(To date, no State systems have been approved under this authority.)

Committee amendment

The Secretary would be authorized to make medicare payments under a State system if five conditions were met—the four in current law, plus the condition that the State system will not preclude HMO's or CMP's from negotiating directly with hospitals with respect to payments for inpatient hospital services. In approving new waivers for State systems, the Secretary would be prohibited from (1) denying an application of a State on the grounds that the State's system is based on a payment methodology other than DRGs or (2) requiring that payments made for medicare patients under the State's system be less than the payments which would have been made under the Federal prospective payment system.

If the Secretary determines that the test of whether or not a State system is resulting in medicare payments in excess of what would otherwise have been paid under the Federal system is based on the State maintaining a rate of increase in payments for medicare hospital inpatient services at no more than a specified percentage increase above a base payment amount for such services, then the State has the option of applying such test either on an aggregate payment basis or on the basis of the payment amount per inpatient discharge on admission. If the Secretary determines that the test is based on the State maintaining a rate of increase in aggregate payments for medicare hospital inpatient services compared to a national percentage increase in total payments for such services, the Secretary cannot deny a State's application for a waiver on the ground that State's rate of increase in such payments must be less than the national average rate of increase.

For existing State systems, the Secretary must judge their effectiveness on the basis of their rate of increase or inflation in medicare inpatient hospital payments compared to the national rate of increase or inflation for such payments. The State would retain the option to have the test applied during the transition period (3 years) on the basis of either aggregate payments or payments per inpatient admission or discharge. After the transition period, this test would no longer apply, and such State systems would be treated in the same fashion as other waivered systems.

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If, subsequent to implementation of a State program, the Secretary determines that the amounts paid over a three-year period under a State system exceed what medicare would have otherwise paid over the same three-year period, the Secretary may reduce subsequent payments to hospitals under the State system by that amount.

For those States which currently have a medicare waiver, the Secretary would be required to continue the State program, if, and for so long as, the five conditions noted above are met.

The committee amendment provides that the Secretary would, upon request of a State, modify the terms of the current demonstration agreement that provides that the State's rate of increase in medicare hospital costs be 1.5 percent below the national rate of increase in medicare hospital costs.

Under the committee amendment, the Secretary would be required to approve any State plan which meets the following requirements in addition to those that are included in the current law and the one noted above: that the system (1) is operated directly by the State or an entity designated by State law; (2) is prospective; (3) provides for hospitals to make such reports as the Secretary requires; (4) provides satisfactory assurances that it will not result in admission practices which will reduce treatment to low-income, high cost, or emergency patients; (5) will not reduce payments without 60 days' notice to the Secretary and to hospitals; and (6) provides satisfactory assurances that in the development of the system, the State has consulted with local governmental officials concerning the impact of the system on public hospitals. The Secretary would be required to respond to requests from States applying under these eleven conditions within 60 days of the date the request is submitted to the Secretary.

8. Administrative and judicial review

Present law

Under current law, a provider may request administrative review By the Provider Reimbursement Review Board (PRRB) of a final decision of a fiscal intermediary regarding ties on the provider cost report, subject to certain conditions. A provider may appeal the PRRB decision to Federal court or, where it involves a question of law or regulation which the PRRB does not have the authority to review, the provider may appeal directly to Federal court.

Committee amendment

The committee amendment would provide for the same procedures for administrative and judicial review of payments under the prospective system as is currently provided for cost-based payments. In general, the same conditions, which now apply for review by the PRRB and the courts, would continue to apply.

With respect to administrative and judicial review, your Committee's bill would permit review except in the narrow cases necessary to maintain budget neutrality and avoid adversely affecting the establishment of the diagnosis related groups, the methodology for the classification of discharges within such groups, and the appropriate weighting of such groups.

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The committee amendment also permits action to be brought jointly by several providers in a judicial district in which the greatest number of such providers are located. Any appeals for judicial review brought by providers which are under common ownership or control would have to be brought as a group, with the PRRB or the district court, in any appeal involving an issue common to such providers.

9. Studies and reports

Present law

Current law directed the Secretary to develop and report to Congress on proposals to reimburse hospitals, skilled nursing facilities, and, to the extent possible, other providers on a prospective basis.

Committee amendment

The committee amendment requires the Secretary to conduct studies and to report to Congress on the following:

(a) Report annually, through fiscal year 1987, on the progress of implementation and the impact of the payment methodology on classes of hospitals, beneficiaries, other classes of payers for inpatient hospital services, and other providers.

(b) Collect the data necessary to determine the relationship between physician charges and inpatient services, and report to Congress by January 1985 with legislative recommendation for prospective payments for physician services based on a DRG-type classification of cases. In addition, the Secretary is directed to examine ways to assure that information is transferred between parts A and B of the program, particularly with respect to those cases when a denial of coverage is made under part A, thereby raising questions about the appropriateness of the reimbursement claimed under part B by an attending physician or physicians.

(c) Study the application of severity of illness, intensity of care, or such other modifications to the diagnosis related groups and report to the Congress by December 1985 on the advisability and feasibility of providing for the application of such modifications. In addition, the Secretary should report on the appropriate treatment of uncompensated care costs and adjustments that might be appropriate for large teaching hospitals located in rural areas.

(d) Report on the feasibility and impact of eliminating separate urban and rural prospective payment rates of applying the prospective system to all payers, and the advisability of having hospitals make available information on the levels of payments accepted by both public programs and by classes of private payers.

(e) The Secretary will continue hospital demonstrations in areas with critical shortages of skilled nursing facilities to study the feasibility of providing alternative systems of care or of methods of payment. The Secretary is also directed to approve a continuation for the On Lok demonstration.

(f) Study the severity of illness and intensity of care differences between hospital and community-based skilled nursing

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facilities (SNFs), and make recommendations with respect to SNF payment by December 31, 1983. In addition, the committee amendment delays for one year the implementation of section 102 of TEFRA concerning a single reimbursement limit for skilled nursing facilities.

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TITLE IV OF THE BILL

Unemployment Compensation Provisions

EXTENSION OF FEDERAL SUPPLEMENTAL COMPENSATION (FSC) PROGRAM

(Section 401 of the Bill)

Present law

The Tax Equity and Fiscal Responsibility Act of 1982 (Public Law 97-248) established the FSC program. This program provides additional weeks of unemployment compensation at the same weekly benefit amount to individuals who have exhausted their State benefits and any extended benefits to which they were entitled. The FSC program, which became effective on September 12, 1982, expires March 31, 1983.

As originally enacted, the FSC program provided 10, 8, or 6 additional weeks of benefits. The Surface Transportation Assistance Act of 1982 (Public Law 97-424) increased the maximum number of weeks of FSC benefits to 16, 14, 12, or 8, depending on the State where the individual filed for or received the additional benefits.

Beginning with the week of January 9, 1983, the FSC program began providing the following maximum weeks of benefits:

(1) 16 weeks in States with an insured unemployment rate (IUR) of at least 6.0 percent (measured as the average over a moving 13 week period);

(2) 14 weeks in States that were triggered on the extended benefits program between June 1, 1982 and January 6, 1983;

(3) 12 weeks in remaining States with a 13 week average IUR of at least 4.5 percent;

(4) 10 weeks in remaining States with a 13 week average IUR of at least 3.5 through 4.4 percent; and

(5) 8 weeks in all other States.

In order to qualify for FSC, a worker must have worked at least 20 weeks or earned its equivalent in wages in his base year, usually defined as the first four of the last five completed calendar quarters before he filed his claim for regular State benefits. He must also have exhausted the regular and extended benefits to which he is entitled. In addition, his benefit year must have ended on or after June 1, 1982 or he must have been eligible for extended benefits for any week beginning on or after June 1, 1982.

If an individual is eligible for FSC benefits, the number of weeks of FSC he may receive is determined in relation to the number of weeks of regular State benefits to which he was entitled. An eligible individual may receive FSC for the lesser of (a) 65 percent of the number of weeks of regular State benefits to which he was entitled or (b) the maximum number of weeks of FSC benefits pro-

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vided in the State. In the case of an interstate claim for FSC, the individual is eligible for the lesser of (a) the maximum number of weeks of FSC payable to him in the State in which he receives the benefits or (b) the maximum number of weeks payable to him in his former State.

Committee amendment

The committee amendment would extend FSC for 6 months from April 1, 1983 through September 30, 1983. To qualify for FSC, an individual would need at least 26 weeks of work or its equivalent in wages in his base year. This restriction would apply only to claimants who initially become eligible for FSC on or after April 1, 1983.

The number of weeks available in each State would be:

(1) *Basic FSC Benefits.*—Individuals who begin receiving FSC on or after April 1, 1983 could receive up to a maximum of:

(1) 14 weeks in States with IUR at 6 percent and above;

(2) 12 weeks in States with IUR at 5 percent to 5.9 percent;

(3) 10 weeks in States with IUR at 4 percent to 4.9 percent; and

(4) 8 weeks in all other States.

No State would, however, lose more than 4 weeks when compared to present law.

(2) *Additional FSC Benefits.*—Individuals who exhaust FSC before April 1, 1983 could receive additional weeks of FSC benefits up to a maximum of:

(1) 8 weeks in States with IUR at 6 percent and above

(2) 6 weeks in States with IUR at 5 percent to 5.9 percent

(3) 4 weeks in States with IUR at 4 percent to 4.9 percent

(4) 4 weeks in all other States.

(3) *Transitional FSC Benefits.*—Individuals who begin receiving FSC before April 1, 1983 and have some FSC entitlement remaining after that date, could also receive additional weeks under (b) above. However, the combination of their remaining basic FSC entitlement received after April 1, 1983, and the additional weeks provided in (b), cannot exceed the maximum number of weeks of basic FSC benefits payable in the State, shown in (a) above.

(4) *Phaseout FSC Benefits.*—Individuals who have not exhausted their FSC entitlement on September 30, 1983 when the program expires, would be eligible to receive up to 50 percent of their remaining FSC entitlement. No new claimants would be added to the FSC program on or after September 30, 1983.

Effective date.—For weeks beginning after April 1, 1983.

OPTIONAL EXCLUSION FROM DISQUALIFICATION FOR NOT ACTIVELY SEEKING WORK UNDER EXTENDED BENEFITS AND FEDERAL SUPPLEMENTAL COMPENSATION FOR CLAIMANTS WHO ARE HOSPITALIZED OR SERVING ON JURY DUTY

(Section 422 of the Bill)

Present law

Present law disqualifies claimants from receiving extended Benefits or Federal Supplemental Compensation if they are not actively seeking work. Moreover, the disqualified claimant must go back to

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work for at least 4 weeks and earn at least 4 times his weekly benefit amount before he can qualify again for Extended Benefits or Federal Supplemental Compensation.

Committee amendment

The committee amendment would permit States to determine on a weekly basis the eligibility availability of claimants of Extended Benefits and Federal Supplemental Compensation who are serving on jury duty or are hospitalized for treatment of an emergency or life-threatening condition. A State must treat these individuals in accordance with their own State unemployement compensation law.

Effective date.—Date of enactment.

DENIAL OF BENEFITS TO NONPROFESSIONAL EMPLOYEES OF EDUCATIONAL INSTITUTIONS BETWEEN ACADEMIC YEARS OR TERMS

Present law

The Federal Unemployment Tax Act (FUTA) covers employees of educational institutions. FUTA requires States to deny benefits between academic years or terms to certain professional employees working in instructional, research, and principal administrative capacities if they have a reasonable assurance of returning to work in the next academic year or term. FUTA gives the States the option of the same denial of benefits, however, for nonprofessional employees of educational institutions.

Committee amendment

The committee amendment would make the denial of benefits between academic years or terms to nonprofessional employees mandatory if the employees have a reasonable assurance of returning to work in the next academic year or term. In addition, States would be required to deny benefits between terms to individuals performing services on behalf of an educational institution or an educational service agency even though not employed by either the institution or agency.

Effective date

The provision would be effective on or after October 1, 1984. States in which there is no legislative session before that date would, however, be given additional time to comply with this provision.

MODIFICATION OF CREDIT REDUCTION CAP PROVISIONS

Present law

Employers in all States currently pay the tax levied under the Federal Unemployment Tax Act (FUTA) at a rate of 3.5 percent on a taxable wage base of $7,000. However, employers in States generally received a FUTA tax credit of 2.7 percent, resulting in a net Federal tax rate of 0.8 percent. Prior to reforms enacted in the Omnibus Budget Reconciliation Act of 1981, State UC programs could borrow on an interest-free basis from the Federal Unemployment Account. However, once a State defaulted on its loans from the

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Federal account, employers in the State began to lose the FUTA tax credit at the rate of a least .3 percent a year.

Specifically, if an advance is not entirely repaid by the State by the second January 1 after the State receives the loan and remains unpaid on the following November 10 of that year, the FUTA tax credit applicable for that year for the State's employers is reduced by .3 percent. For each succeeding year in which the loan remains outstanding, the reduction is at least an additional .3 percent (i.e., .6, .9, 1.2 percent, etc.). Additional offset credit reductions may apply to a State beginning in the second year of repayment if certain criteria are not met. Under legislation enacted in the 1970's, credit reductions were not imposed from 1975–1980 for States satisfying specific requirements. Sixteen states are experiencing a credit reduction for 1983.

The 1981 Budget Reconciliation Act made two major changes in loan repayment conditions: interest of up to 10 percent is charged on loans made after April 1, 1982 (except those made for "cash flow" purposes and repaid by the end of the fiscal year in which they occur); and States are allowed to "cap" the automatic FUTA credit reductions if certain solvency requirements are met.

For a State qualifying for the cap, the annual tax credit reduction is limited to 0.6 percent, or the rate that was in effect for the State for the preceding calendar year, whichever is higher. These loan reform provisions are in effect from January 1, 1981 to December 31, 1987.

The cap provisions are designed to give States additional time to make legislative and administrative changes necessary to restore the State trust funds to solvency. These provisions lengthen the repayment period, but do not reduce a State's total liability.

In order to qualify for the cap on the FUTA penalty tax a State must demonstrate that:

(1) the net solvency of its UI system has not diminished (effective for taxable years 1981–1987);

(2) there have been no decreases in its unemployment tax effort (effective for taxable years 1981–1987);

(3) its average tax rate for the calendar year equals or exceeds its average benefit cost rate for the prior five years (effective for taxable years 1983–1987; and

(4) the outstanding loan balance as of September 30 of the tax year in question is not greater than on the third preceding taxable year (effective for taxable years 1983–1987). The comparable year for taxable year 1983, however, is 1981.

Committee amendment

The committee amendment would make the credit reduction cap: provisions in present law permanent. A State would still be required to meet all four conditions in present law to qualify for the credit reduction cap in present law. The committee amendment would, however, provide two possible lower credit reductions, if a State does not qualify for the total cap: (1) If a State meets the first two present law credit reduction cap conditions and either of the remaining two conditions, the credit reduction would be 0.2 instead of at least 0.3 percentage points; and (2) If a State meets the first two credit reduction cap conditions and qualifies for the interest

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deferral authorized as a result of substantial changes in its unemployment compensation law, the credit reduction would be 0.1 instead of at least 0.3 percentage points. The lower credit reductions would be authorized only for taxable years 1983, 1984, and 1985 liabilities.

The January 1st of each year for which a State qualifies for a partial limitation on the offset credit reduction will be taken into account for purposes of determining future offset credit reductions. The credit reduction applicable in each subsequent year after the partial limitation is in effect would continue to be reduced by the amount by which the offset credit was reduced.

Effective date.—Date of enactment.

MODIFICATION OF INTEREST PROVISIONS

Present law

Present law imposes interest of up to 10 percent per year on loans obtained by the States after April 1, 1982, except for "cash flow" loans that States repay by the end of the fiscal year in which the loans were obtained. A State can defer payment of its interest due for the fiscal year by paying 25 percent in each of four years beginning with the year in which the interest is due. Interest accrues, however, on the deferred interest.

Committee amendment

The committee amendment would make the provisions imposing interest on the States permanent. It would also provide for another deferral and a discounted interest rate for which States could apply if they meet certain conditions as certified by the Secretary of Labor.

The new deferral would be 80 percent of the amount due for the fiscal year. It would be authorized for interest accrued only for fiscal years 1983, 1984, and 1985. The deferred amount would be payable in 4 installments in the succeeding years equal to at least 20 percent of the original amount of interest due. A State would be required to meet two conditions to qualify for the deferral:

(1) no action has been taken to reduce its tax effort or trust fund solvency; and

(2) action (certified by the Secretary of Labor) after October 1, 1982, has been taken which would increase revenues and decrease benefits by a total of 30 percent in the calendar year immediately following the fiscal year for which the first deferral is requested. Deferral in the years immediately following the year in which the first year change is effective may be received if changes of 40 and 50 percent are made.

The discounted interest rate would be one percentage point below the interest rate that would otherwise apply. It would be authorized for interest accrued only for fiscal years 1983, 1984, and 1985. It would be available under the same conditions as the new deferral above, except the required percentage changes in (2) would be higher at 50, 80, and 90 percent, respectively.

For purposes of determining whether a State meets the conditions in (2) above, the Secretary of Labor will provide an estimate of the unemployment rate for the base year, the calendar year in

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which the deferral is requested. The level of benefits and revenue liabilities will be determined using the State law in effect before passage of the legislation. The estimate of changes as a result of new legislation will be made from the base year in each year for which a deferral is requested. Once a deferral is approved, a State must continue to maintain its solvency effort. Failure to do so would result in immediate payment of all deferred interest.

Increases in the taxable wage base from $6,000 to $7,000 after calendar year 1982 and increases in the maximum tax rate to 5.4 percent after calendar year 1984 will not be counted for purposes of meeting condition (2).

States will not be penalized or rewarded if economic events change from those used in the base year for computing eligibility under condition (2).

Effective date.—Date of enactment.

CHANGE IN SECOND YEAR ADDITIONAL CREDIT REDUCTION

Present law

Present law provides that a State, in the second year in which the offset credit reduction is imposed to repay outstanding loans, may be subject to an additional credit reduction equal to the amount by which the State's average tax rate is lower than 2.7 percent. The average tax rate and the 2.7 percent are computed from the ratio of taxes collected to State and Federal taxable wages, respectively. Taxable wages are determined by the taxable wage base. Any wages above the taxable wage base are therefore not included.

In States where the taxable wage base exceeds the Federal taxable wage base of $7,000, the tax rate base on the State's taxable wages will be lower than it would be if their taxable wage bases were $7,000. This could activate the additional credit reduction in the second year even though these States have relatively higher tax efforts.

Committee amendment

The committee amendment would change the computation of the average tax rate to reflect the ratio of the federal unemployment tax base to the national average wage in covered employment.

Effective date.—Taxable year 1983.

CHANGE IN THE DATE INTEREST IS DUE

Present law

Present law requires that interest is due no later than the first day of the next fiscal year. If the first day of the next fiscal year falls on a weekend, interest is due in the prior fiscal year. Otherwise, it is due on the first day of the next fiscal year.

Committee amendment

The committee amendment requires that interest be paid before the first day of the next fiscal year.

Effective date.—Date of enactment.

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COLLECTION INTEREST

Present law

Present law provides no mechanism through which the Federal Government can collect interest from the States if the States do not pay interest when it is due.

Committee amendment

The committee amendment would require the collection of delinquent interest charges one year after they are due by a reduction in the FUTA credit of 0.1 percentage point. Any amount collected during the imposition of this provision exceeding the overdue interest would be applied to the outstanding loan as an involuntary repayment. This provision would provide a specific collection mechanism to assure the payment of interest pending completion of any conformity proceeding which is implicitly but clearly required for nonpayment of interest by a State.

Effective date.—Date of enactment.

COSTS OF CARRYING OUT THE PROVISIONS OF THE BILL

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, D.C., March 11, 1983.

Hon. ROBERT J. DOLE,
Chairman, Committee on Finance,
Washington, D.C.

DEAR MR. CHAIRMAN: Pursuant to Section 403 of the Congressional Budget Act of 1974, the Congressional Budget Office has prepared the attached cost estimate for S.1, the Social Security Act Amendments of 1983, as ordered reported by the Senate Committee on Finance on March 10, 1983,

Should the Committee so desire, we would be pleased to provide further details on this estimate.

Sincerely,

JAMES BLUM
(For Alice M. Rivlin, Director).

CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

1. Bill number: S. 1.
2. Bill title: Social Security Act Amendments of 1983.
3. Bill status: As ordered reported by the Senate Committee on Finance on March 10, 1983.
4. Bill purpose: To amend the Social Security Act to assure the solvency of the Social Security trust funds; to accelerate presently scheduled payroll tax increases; to tax 50 percent of certain individuals' benefits; to increase the self-employed tax; to delay the payment of cost-of-living adjustments; to reform the Medicare reimbursement of hospitals; to extend the federal supplemental compensation program; and for other purposes.

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5. Estimated cost to the Federal Government: The following table shows the estimated costs of this bill to the federal government.

Because no draft language has been received, CBO cannot estimate certain provisions in this bill at this time. These provisions relate to the Unemployment Insurance and SSI programs. The cost estimate for the remaining provisions present the best estimates based on current information.

TABLE 1.—ESTIMATED BUDGET AUTHORITY, OUTLAY, AND REVENUE IMPACTS OF S. 1, THE SOCIAL SECURITY ACT AMENDMENTS OF 1983

[By fiscal year, in millions of dollars]

	1983	1984	1985	1986	1987	1988
Spending:						
Function 550:						
Budget authority	3,439	1,001	1,985	2,283	2,665	2,987
Outlays	105	93	33	−131	−135	140
Function 600:						
Budget authority	22,235	14,084	14,713	14,503	16,673	30,457
Outlays	341	−3,067	−3,447	−3,626	3,764	−4,140
Function 700:						
Budget authority	0	−89	−58	−58	60	−63
Outlays	−25	−54	58	−58	−60	63
Total spending:						
Budget authority	25,675	14,996	16,640	16,728	19,278	33,381
Outlays	421	−3,028	−3,538	−3,815	−3,959	−4,343
Revenues	0	6,466	7,579	7,453	8,889	19,825
Change in unified budget deficit	421	−9,494	−11,117	−11,268	−12,848	−24,168

The spending effects of this bill fall within budget functions 550, 600 and 700. The budget authority is the net result of higher interest income on higher trust fund balances for the Old Age Survivors Insurance (OASI), the Disability Insurance (DI) and Hospital Insurance (HI) programs, transfers to the trust funds from the general fund of the U.S. Treasury, and required additional budget authority for the Supplemental Security Income (SSI), Supplementary Medical Insurance (SMI), Food Stamps, Veteran's Pensions and Medicaid programs.

Basis of estimate: This bill generally incorporates the January, 1983 recommendations of the National Commission on Social Security Reform. It also incorporates provisions affecting the Medicare, Supplemental Security Income and Unemployment Insurance Programs. Table 2, shows the costs, savings and revenue impacts of this bill to the federal government.

One major purpose of this bill is to ensure the continued payment of all Social Security benefits. The impact of some of the provisions in the bill on the financial status of the Social Security trust funds differs from their impact on the federal budget. Many provisions transfer funds within the government, which has no impact on budget outlays or receipts. In addition, the savings to and income into the trust funds generate additional interest income or budget authority. This income also does not affect the unified budget deficit. The impact of the bill on the trust funds therefore is shown separately in Table 3.

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TABLE 2.—ESTIMATED OUTLAY AND REVENUE CHANGES TO THE UNIFIED FEDERAL BUDGET RESULTING FROM S. 1, THE SOCIAL SECURITY ACT AMENDMENTS OF 1983

[By fiscal year, in millions of dollars]

	1983	1984	1985	1986	1987	1988
Outlay changes:						
Delay COLA 6 months:						
OASDI	−7,704	−3,793	−4,228	−4,473	−4,706	−5,181
SSI	−100	−130	−170	−170	−175	−210
Veterans' Pensions	−25	−54	−58	−58	−60	−63
Offset: Food stamps	0	37	46	51	53	53
Medicare premium delay:						
SMI	114	63	−90	−201	−206	−211
HI	1	([1])	([1])	([1])	([1])	([1])
Offset: Medicaid	−9	−5	7	15	16	16
Increase SSI benefits: SSI	250	750	845	840	875	935
Offsets:						
Food stamps	−40	−165	−170	−170	−175	−175
Medicaid	0	35	50	55	55	55
Extend FSC program for 6 months:[2]						
Unemployment compensation	2,070	120	0	0	0	0
Offsets to food stamps and AFDC	−135	−8	0	0	0	0
Prospective payment system	0	0	0	([3])	([3])	([3])
State waiver change	0	([4])	([4])	([4])	([4])	([4])
Miscellaneous outlay impacts:						
OASDI	0	122	230	296	364	438
SSI and AFDC	([5])	([5])	([5])	([5])	([5])	([5])
Total outlay changes	421	−3,028	−3,538	−3,815	−3,959	−4,343
Revenue changes						
FICA increase:						
OASDI	0	6,361	2,349	0	0	10,272
Railroad retirement	0	45	0	0	0	61
1984 FICA Tax Credit	0	−3,240	−985	0	0	0
Other FICA Tax Offsets	0	−795	−147	0	0	−1,284
SECA tax increase	0	1,408	4,304	4,382	4,747	5,199
SECA Tax Credit	0	−893	−2,645	−2,481	−2,397	−2,447
Cover nonprofit employees	0	1,118	1,697	1,955	2,297	2,853
Nonprofit workers income tax offsets	0	−141	−212	−244	−287	−357
Cover new Federal workers	0	61	185	315	455	636
State speedup	0	1,600	200	136	104	200
Tax 50 percent of benefits						
OASDI	0	780	2,769	3,316	3,885	4,594
Railroad Retirement	0	20	64	74	85	98
Increased tax revenues from FSC extension[2]	0	142	0	0	0	0
Total revenue changes	0	6,466	7,579	7,453	8,889	19,825
Total impact on united budget deficit	421	−9,494	−11,117	−11,268	−12,848	−24,168

[1] Less than $0.5 million.

[2] This bill contains no estimates relating to unemployment trust fund loan reform.

[3] The budgetary impact cannot be estimated because the bill would allow the Secretary of Health and Human Services, as advised by a panel of experts, nearly unlimited discretion in setting payment rates for inpatient hospital services. Those rates could be set such that Medicare outlays in the aggregate would increase or decrease.

[4] The cost of this provision cannot be estimated becaue it depends on the actions of state hospital rate-setting commissions in Massachusetts and New York.

[5] SSI costs do not include costs of the provision requiring notices to be sent to social security beneficiaries informing them about SSI. See the text for details.

Source CBO estimates based on February, 1983 economic assumptions.

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TABLE 3.—ESTIMATED CHANGES IN OASI, DI AND HI TRUST FUND OUTLAYS AND INCOME RESULTING FROM S. 1, THE SOCIAL SECURITY ACT AMENDMENTS OF 1983

[By fiscal years, in millions of dollars]

	1983	1984	1985	1986	1987	1988
Trust fund outlay changes:						
6-month COLA delay:						
OASI	−1,519	−3,394	−3,805	−4,049	4,272	4,712
DI	−185	−399	−423	−424	−434	−469
Miscellaneous provisions:						
OASI	0	122	230	296	364	438
Total outlay changes:						
OASI	−1,519	3,272	−3,575	3,753	−3,908	4,274
DI	−185	−399	−423	424	434	469
Total	−1,704	−3,671	−3,998	-4,177	−4,342	−4,743
Trust fund income changes:						
Tax 50 percent of benefits: OASI[2]	0	780	2,769	3,316	3,885	4,594
FICA tax speedup:						
OASI	0	5,476	1,974	0	0	8,631
DI	0	966	403	0	0	1,764
SECA tax increase:						
OASI	0	856	2,525	2,447	2,608	2,912
DI	0	175	517	501	534	597
HI	0	377	1,262	1,434	1,605	1,670
Cover newly hired Federal workers:						
OASI	0	104	314	536	774	1,081
DI	0	18	56	94	136	191
Cover non-profit organizations:						
OASI	0	712	1,083	1,226	1,427	1,763
DI	0	189	288	332	390	485
HI	0	216	326	397	480	605
Military transfer credits:						
OASI	16,800	−380	−385	−210	220	210
DI	2,300	−60	−60	−35	35	35
HI	3,290	−70	−70	60	60	60
Uncashed checks:						
OASI	680	43	43	43	43	43
DI	120	7	7	7	7	7
State speedup: OASDHI	0	1,600	200	136	104	200
Total income changes:						
OASDI	19,900	10,487	9,734	8,393	9,653	22,023
HI	3,290	523	1,518	1,771	2,025	2,215
Total	23,190	11,010	11,252	10,164	11,678	24,238
Total outlay and income infusions to trust funds:						
OASDI	21,604	14,158	13,732	12,570	13,995	26,761
OASDHI	24,894	14,681	15,250	14,341	16,020	28,981
Estimated interest income						
OASDI	290	2,948	4,428	5,559	6,442	7,770
OASDHI	335	3,333	4,928	6,202	7,217	8,682
Total annual increase in trust funds:						
OASDI	21,894	17,106	18,160	18,129	20,437	34,531
OASDHI	25,229	18,014	20,178	20,543	23,237	37,663

[1] Assumes no reallocation between OASI and DI trust funds
[2] Assumes all revenues allocated to OASI trust fund.

Source CBO estimates based on February 1983 economic assumptions

A Section by section description for the basis of the estimates for the provisions in this bill having major cost impact is given below.

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These estimates were prepared from a draft of the bill before Committee amendments were added and from mark-up documents. No bill as amended has been received.

PROVISIONS AFFECTING THE FINANCING OF THE SOCIAL SECURITY SYSTEM

Cover new Federal employees

This provision extends Social Security coverage to all new permanent federal civilian employees as of January 1, 1984. The proposal is expected to cover about 150,000 new permanent federal entrants per year through 1988. The proposal raises $61 million in unified budget revenues in fiscal year 1984 and $1.7 billion in revenues from fiscal year 1984 through 1988.

This provision assumes no change in the current Civil Service Retirement system for those federal workers newly covered by Social Security. No impact of any Civil Service change is given in this estimate.

The estimate is based on CBO's current economic and federal employment assumptions.

Cover workers in non-profit organizations

The provision requires mandatory coverage of all employees of non-profit institutions and organizations. Approximately 20 percent of employees of non-profit organizations and institutions are not currently covered by Social Security. Covering the last 20 percent of non-profit employees raises $1 billion in fiscal year 1984 and $8.7 billion in fiscal years 1984 through 1988.

The extension of mandatory coverage to all non-profit employees results in an income tax offset against the increase in OASDHI revenues. The offset equals 25 percent of the employer contribution and reduces income tax revenues. Income tax revenues are estimated to fall because it is assumed that non-profit employers pass the entire payroll tax increase onto their employees in the form of lower wages and salaries.

The estimate was based on CBO's economic assumptions using the Social Security Administration's short-term revenue forecasting model.

Termination of State and local coverage

Currently, state and local governments can terminate Social Security coverage upon giving two years notice of their intention to withdraw, and then doing so. This provision would prohibit any such withdrawals, effective with the bill's enactment.

CBO's current law revenue estimates do not assume reductions in trust fund income that could result from withdrawals of certain state and local governments. Thus, there would be no revenue gain to the CBO baseline estimates from prohibiting such withdrawals.

Delay payment of annual cost-of-living adjustment from July to January of each year

This section delays the payment of future cost-of-living adjustments (COLA's) for Social Security for six months, from July to

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January of each year. In addition, the provision changes the base period from which the COLA is calculated.

The COLA is measured by the growth in the Consumer Price Index (CPI) from the first calendar quarter of the previous year to the first quarter of the current year. Whenever the increase is greater than three percent, an adjustment to the benefits paid each July is made. The July, 1983, COLA will be paid in January, 1984 under this provision, and will be based on the current law indexing period. Subsequent adjustments will be based on the CPI growth from the third quarter of one year to the next. The table below shows the CBO COLA assumptions under current law and under this provision.

ASSUMED PERCENTAGE INCREASE IN SOCIAL SECURITY BENEFITS UNDER CURRENT LAW AND UNDER S.1

	1983	1984	1985	1986	1987	1988
Current law—July	4.1	4.6	4.5	4.2	4.0	3.8
Proposed—January	0.0	4.1	4.6	4.4	4.1	3.8

This bill also guarantees that a January, 1984 COLA will be given, even if the rate of inflation is so low that the adjustment is less than three percent. Since CBO's current economic assumptions have this COLA adjustment at 4.1 percent in 1984, this clause has no cost effect.

The change in the COLA base and date of payment is expected to save $24 billion in Social Security benefits over the period, and an additional $1.3 billion in SSI and other benefits directly linked to this COLA. These COLA changes would increase food costs by $240 million over the period as incomes of food stamps recipients decline.

Taxation of 50 percent of social security and railroad retirement benefits for individuals with income above $25,000 and married couples above $32,000

This provision includes in taxpayers' adjusted gross income (AGI) half of Old Age, Survivors and Disability Insurance (OASDI) benefits when those benefits plus AGI exceeds a threshold amount. For the purpose of taxing half of OASDI benefits, the interest from tax free bonds is added to AGI. The threshold is $25,000 for single returns, $32,000 for joint returns, and zero for married couples filing separately. This limit would be calculated including an individual's or couple's tax exempt income, although this income would not count towards determining one's marginal tax rates. The amount of benefits included in AGI would be the lesser of either 50 percent of benefits or the one-half of the balance of the taxpayers' summed income over the threshold.

The provision raises $800 million in fiscal year 1984 and $15.3 billion from fiscal year 1984 through 1988. The revenue effects are derived from the Joint Committee on Taxation estimates based on the Social Security Trustees' II-B assumptions, with benefit amounts lowered to take account of the CBO's lower inflation (and therefore cost-of-living adjustments) projections.

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Increase social security payroll tax (FICA) and 1984 tax credit

The provision accelerates the OASDI payroll tax (FICA) increases for employees and employers. The payroll tax increases to 5.7 percent from 5.4 percent on January 1, 1984 instead of January 1, 1985. Another tax rate speedup increases the rate to 6.06 percent from 5.7 percent on January 1, 1988 and January 1, 1989. This increase was scheduled to take effect in 1990. The proposal also includes a payroll tax credit of 0.3 percent of employee FICA contribution for 1984.

The FICA tax acceleration results in an income tax offset equal to 25 percent of the employer payroll tax contribution. The offset lowers income tax receipts because employers are assumed to pass back onto employees the full payroll tax increase in the form of lower wages and salaries.

The provision is estimated to raise OASDI unified budget revenues $6.4 billion in fiscal year 1984 and $19.0 billion from fiscal year 1984 through fiscal year 1988. The income tax offset equals $2.2 billion from fiscal years 1984 through 1988. The revenue loss due to the payroll tax credit results in a $4.2 billion loss by fiscal year 1985.

The estimates are based upon CBO's latest economic assumptions using the Social Security Administration's short-term revenue forecasting model.

Increase self-employed tax rate

The provision raises the self-employed payroll tax rate (SECA) to a level equal to the combined employer-employee contribution rate (including the FICA tax acceleration). In 1984 the SECA OASDI rate increases 3.35 percent and the HI rate increases 1.3 percent for a SECA rate of 14 percent. Further, the provision includes a payroll tax credit equal to 2.9 percent of total SECA contributions in 1984 and 2.5 percent in 1985, 2.2 percent in 1986, and 2.1 percent in 1987 and 1988.

The proposal raises $1,408 million in SECA revenues in fiscal year 1984 and $20 billion from fiscal year 1984 through 1988. The income tax loss due to the self-employed payroll tax credit equals $893 million in fiscal year 1984 and $10.9 billion from fiscal year 1984 through fiscal year 1988.

Reallocation of OASI and DI tax rates

This provision has no net cost to the federal government. It realigns the payroll tax portions allocated to the OASI and DI trust funds so as to keep the two funds' balances at approximately the same percentage of outlays at the start of each year.

Benefits to certain widows, divorced and disabled women

These provisions would: (1) allow the continuation of benefits to surviving, divorced or disabled spouses who remarry; (2) change the indexing procedure for benefits for those receiving deferred survivor benefits; (3) allow divorced spouses to draw benefits regardless of whether the former spouse is receiving benefits; and (4) increase benefits for disabled widows and widowers.

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Together, these provisions would cost less than $200 million per year once fully effective in fiscal year 1985. The largest cost in this group of provisions would allow disabled widows or widowers ages 50 to 59 to receive benefits at an amount equal to which non-disabled widows or widowers over age 59 currently receive. This provision is estimated to cost $90 million in fiscal year 1984, $125 million in 1985 and an estimated $600 million over the five year period. Based on Social Security Administration data, approximately 200,000 recipients would receive $50 or 20 percent in added benefits per month under this provision.

In addition, a provision in this bill to allow women with children additional years of zero earnings in the calculation of their benefits.

Reimburement to OASDHI trust funds for military wage credits and unearned OASDI checks

These provisions will credit the three Social Security trust funds with $23.8 billion as part of a transfer in 1983 from the general fund of the Treasury. A total of $22.4 billion of this transfer represents the present value of estimated benefits arising from Social Security credits granted to military personnel for service prior to 1957, and the amount of taxes on these credits between 1956 and 1983. The remaining transfer is for the estimated amounts of uncashed Social Security checks for past years. Checks uncashed for longer than six months will also be credited back to the trust funds in future years.

These estimates were provided by the Social Security Administration. Although they add large amounts to the trust funds, the provisions do not have any cost impact to the federal government as a whole. There are offsetting interfund transfers within the federal unified budget.

State payment speedup

This provision will require state and local governments to transfer their payroll tax collections to the Treasury under the same rules as private sector employers. Currently, state payments are made on the 30th day of each month. The provision requires that states transmit payroll tax collections to the federal government soon after their employees are paid. Therefore, the Treasury would receive state FICA collections more frequently. Thus, the transfer to the Treasury would be hastened, adding to trust fund revenues by $1.6 billion in fiscal year 1984 and $2.2 billion over the period.

This estimate was prepared by the Social Security Administration.

LONG-TERM FINANCING

This section of the bill reduced initial benefit levels beginning in the year 2000. There are no effects resulting from these provisions in the 1983 to 1988 period. In addition, the retirement age will be gradually raised from 65 to 66 beginning in the year 2000.

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MISCELLANEOUS PROVISIONS

These provisions are aimed mostly at work incentives for the elderly, and at insuring the financial soundness of the trust funds. The provisions would eliminate the retirement test for workers over the age of 65 beginning in 1990. This test reduces retirement benefits by $1 for each $2 in earnings over a given amount ($6,600 in 1983). A delayed retirement credit of 8 percent would also be phased in. This credit would increase from 3 percent the added benefit amount paid to a retiree for each year a worker decides to retire after age 65.

Another section of the bill would require Congress to act if the balances in the trust funds fall below 20 percent of a year's outlays. If Congress does not, and interfund borrowing (also provided for in the bill) does not achieve this result in each fund, then the cost-of-living adjustments would be altered until the funds recover. The cost-of-living adjustment would be reduced first for those with higher benefits, but those with lower benefits would also ultimately be reduced, if necessary. This cost estimate does not assume any further cost-of-living adjustment reduction beyond the six month delay discussed above.

SUPPLEMENTAL SECURITY INCOME PROVISIONS

This title of the bill raises SSI benefits and makes other minor changes in SSI and AFDC. Together these changes are estimated to add $728 million to federal outlays in fiscal year 1985.

Beginning July 1, 1983, SSI benefits would be increased by $20 a month for individuals living in their own household and by $30 a month for couples. These increased benefits would more than offset the effect on SSI recipients of the COLA delay. The largest part of the added cost comes from the benefit increase for current SSI beneficiaries. In addition, CBO estimates that about 125,000 persons would become new beneficiaries of SSI. Most would be newly eligible for SSI as a result of the increased income limits. For these persons, CBO has assumed a participation rate of 25 percent (that is, of all the newly eligible, 25 percent would actually participate in SSI). Some of the other new beneficiaries would be persons previously eligible who would now choose to participate as a result of the increased benefit levels. There are also an estimated 65,000 persons who were receiving SSI state supplements only who would now become eligible for a small federal SSI payment.

Partially offsetting the costs in SSI from these benefit increases is a savings in the food stamp program as incomes of SSI beneficiaries rise. There are also added costs in Medicaid for those new SSI beneficiaries who also become newly eligible for Medicaid.

This title would also enable temporary residents of emergency public shelters to receive SSI for three months in any twelve-month period. This provision is estimated to cost $1 million in fiscal year 1983 and $3 million a year thereafter. In addition, Title IV would disregard in the determination of benefits any in-kind assistance based on need received by SSI and AFDC beneficiaries. This provision, which is effective only through September 30, 1984, is estimated to cost less than $500,000 a year in SSI and $1 million in 1983 and $2 million in 1984 in AFDC.

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The bill also apparently includes a provision that would require the Social Security Administration to send notices to Social Security beneficiaries informing them of their potential eligibility for SSI and urging them to contact a local office if they think they would be eligible. No language is available for this provision and the extent of the notices could vary considerably. Hence, there is no cost estimate for the provision. However, costs under even a fairly limited provision could be significant, perhaps around $50 million. Not only would there be added administrative costs but it would be reasonable to assume that around 5 percent of those receiving a notice who are eligible for SSI would apply for SSI benefits.

UNEMPLOYMENT COMPENSATION PROVISIONS

Federal supplemental compensation

This section of the bill would extend for six months the federal supplemental compensation program (FSC) now scheduled to terminate March 31, 1983. It would provide up to 14 weeks of additional unemployment compensation benefits for individuals exhausting regular or extended unemployment benefits after March 31, the maximum number of weeks provided varying with a state's insured unemployment rate (IUR). In addition, it would provide those persons who have exhausted their FSC entitlement before March 31 with up to 8 additional weeks of benefits, the maximum number of weeks again varying with a state's IUR. Also, it would allow those persons who have benefit entitlements remaining on September 30, 1983 to receive up to one-half the balance of those entitlements.

The estimate of the fiscal impact of this section of the bill is based upon estimates of the states' IURs and weeks compensated, and the determination of whether a state will be paying extended benefits which underlies the CBO baseline. It is assumed that the national seasonally adjusted IUR will be 4.4 percent for both quarters of the extension. Furthermore, it is assumed that 45 percent of those claimants in the current law FSC program would exhaust and collect added weeks of benefits during the extension. This point estimate is based upon the experience of exhaustees of the federal supplemental benefits program of 1975 to 1978.

CBO estimates that any FSC extension results in a reduction in AFDC and Food Stamp outlays as individuals who exhaust unemployment benefits and would otherwise draw benefits from these means-tested programs continue to draw jobless payments. It is estimated that the extension through September 1983 will cause AFDC and food stamp expenditures to drop by $142 million. In addition, CBO estimates that the six-month FSC extension will cause income tax revenues to increase in fiscal year 1984 by $142 million.

Loan reform

This bill contains a provision relating to limiting the federal tax credit reduction and to paying interest of federal unemployment compensation loans to states. CBO has provided no estimates of the fiscal impact of these provisions.

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MEDICARE HOSPITAL INSURANCE PROVISIONS

Conforming changes in medicare premiums

The bill would postpone from July 1 to January 1 of the following year increases in Medicare premiums. Current premium amounts would apply during the interim. Future premiums (and the general revenue contribution to SMI) would be calculated on the basis of estimated incurred costs for the calendar year during which the premium would apply. Consonant with the changes made by TEFRA a year ago, SMI premiums would be set at 25 percent of cost per aged enrollee in calendar year 1984 and 1985, but would be limited in subsequent years by the cost-of-living increase in social security benefits in the previous January.

The estimated costs of this provision are the difference between projections of income from premiums under current law and under the amendment. Premium income under the amendment is the product of monthly enrollment projections and monthly premium amounts computed on the basis of projected incurred costs by calendar year.

General.—The bill would provide for reimbursing most hospitals for inpatient services provided to Medicare enrollees on the basis of payment amounts, varying by diagnosis, fixed in advance of the period in which they would apply. The provision would be effective with hospital cost-reporting periods beginning on or after October 1, 1983. With the exceptions discussed below, for the first two cost-reporting periods affected, the payment rates would be set to assure that total Medicare payments for inpatient hospital services in affected hospitals would be neither greater nor less than under current law. If implemented faithfully, the provision would have no budgetary impact in fiscal years 1984 and 1985. In subsequent fiscal years, however, the Secretary of Health and Human Services, advised by a panel of experts, would have nearly unlimited discretion in setting payment rates. Given that discretion, CBO is unable to determine whether the prospective payment provision would result in federal costs or savings after fiscal year 1985.

The proposed mandatory Social Security coverage of employees of non-profit organizations could raise labor costs for some hospitals. Under the bill, Medicare's share of any such costs would be additional costs to the Medicare program. CBO is unable to estimate those costs at this time.

Change in State Waiver Requirement.—The bill would phase out the requirement that the rate of increase in Medicare hospital costs in states currently reimbursing hospitals under demonstration agreements entered into after August 1982 be less than the national rate of increase in those costs. The provision would affect only Massachusetts and New York, both of which operate hospital rate-setting programs that have for several years held their hospital cost increases well below the national average. If those states were to continue to be as successful as they have been, the provision would have no budgetary impact. On the other hand, the provision would allow larger cost increases than current law. If Medicare hospital costs were to rise one percentage point faster under the provision, federal spending would increase by about $50 million in 1984.

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6. Estimated cost to State and local governments: A number of the provisions of this bill would affect budgets of state and local governments. Their estimated net impact on categories of state and local expenditures is shown in the table below.

TABLE 4.—ESTIMATED COST TO STATE AND LOCAL GOVERNMENTS

	1983	1984	1985	1986	1987	1988
Payroll costs		291	159			446
Speedup of FICA deposits		800	105	73	57	105
SSI State supplements	35	120	130	125	125	130
Medicaid	−8	26	49	60	60	60
AFDC	−29	1				
General assistance	−13					
Total	−15	1,238	443	258	242	741

Basis of estimate: The acceleration of FICA rate increases would add to state and local government payroll costs. Currently, about 70 percent of total state and local government employment is covered by Social Security. State and local governments would have added payroll tax contributions of $291 million in fiscal year 1984 and $896 million over the entire 1984–88 period. The CBO estimate does not include a future cost to states who would no longer be able to withdraw from the Social Security system under this legislation.

The provision speeding up FICA deposits would require state and local governments to forward their FICA deposits about one month earlier. In the first fiscal year following enactment, states would show higher budgetary outlays for their (the employers') share of the FICA deposits which is one-half of the total savings shown for the federal government. In addition, state and local governments would lose small amounts of interest they would otherwise have earned on the balances over a one month period.

The changes in SSI would increase state and local government costs. Virtually all states supplement federal SSI benefits. The $20 benefit increase would raise state costs unless states were to lower their state supplement benefit levels. Typically, lowering of benefit levels requires action by state legislatures. The CBO cost estimate assumes that current state supplement levels remain in effect. Consequently, it represents a maximum cost to state and local governments.

The CBO cost estimate for the $20 benefit increase incorporates added costs to states and localities for current state supplement only beneficiaries, for new state supplement beneficiaries as a result of the new federal beneficiaries (about one-third of federal SSI beneficiaries receive state supplements), and for new state supplement only beneficiaries who are newly eligible. Costs of this provision are estimated to total $124 million in fiscal year 1985.

In addition to the effect of the $20 benefit increase, SSI state supplement costs would be increased by the COLA delays in SSI and OASDI. When COLAs are made, state supplement costs decline slightly because for state supplement only beneficiaries OASDI in-

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creases are larger than SSI increases. The costs of the COLA delays are estimated to total about $6 million a year.

The CBO cost estimate does not include any cost effect of the altered "pass-through" requirements of section 402. Current law requires states to pass through to SSI beneficiaries federal benefit increases unless state payment levels are above their December 1976 levels or unless aggregate state SSI supplement expenditures in the 12 months following a federal payment level increase exceed aggregate state expenditures in the 12 months prior to the federal change. This provision would require states to pass through the dollar amount of the COLA that would have occurred in July 1983 under current law and also all future federal benefit increases, even if state payment levels are above the December 1976 levels. Hence, in future years the provision would limit the flexibility of states to reduce supplement levels when federal SSI benefits increase, raising costs for some states. However, for other states—those with payment levels equal to their December 1976 levels—this provision would result in potential savings because they could pass through the July 1983 cost-of-living adjustment amount (roughly $11) rather than the full $20 benefit increase.

Expenditures of state and local governments would also rise because of higher Medicaid costs occasioned by the SSI benefit increase and the Medicare premium delay discussed earlier. The state and local government financing share of Medicaid averages about 46 percent.

The increased federal supplemental compensation benefits for the unemployed would lower state and local government expenditures in two ways. First, AFDC outlays would decline in fiscal year 1983. The state share of such outlays averages 46 percent. Second, outlays for state and local general assistance (GA) programs would also decline. GA programs are fully funded by state and local governments and are means-tested, typically serving those ineligible for AFDC and SSI. There are no reliable statistics on which to base an estimate of savings in GA. However, a rough estimate of the estimated effect in Michigan provided by Michigan analysts was used to estimate national effects. Michigan accounts for about 15 percent of GA expenditures nationwide.

7. Estimate comparison: None.

8. Previous CBO estimate: None.

9. Estimate prepared by: Stephen Chaikind, Malcolm Curtis, Richard Hendrix, John Navratil, Janice Peskin, Roger Hitchner, Kathleen Shepherd (226-2820), James Nason (226-2689).

10. Estimate approved by:

C. G. Nuckols
(For James L. Blum, Assistant Director for Budget Analysis).

Vote of the Committee

In compliance with paragraph 7(c) of Rule XXVI of the Standing Rules of the Senate, the following statement is made relative to the vote by the committee on the motion to report the bill S. 1, as amended, was ordered favorably reported by a vote of 18 yeas, 1 nay.

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Regulatory Impact Statement

Because of the urgent nature of this legislation and the necessity for prompt action to assure the financial solvency of the social security program, it is necessary to dispense with the requirements of paragraph 12 of Rule XXVI of the Standing Rules of the Senate relating to regulatory impact statements as is provided for in the last sentence of such paragraph.

Changes in Existing Law Made by the Revenue Provisions of the Bill as Reported

In the opinion of the committee, it is necessary in order to expedite the business of the Senate, to dispense with the requirements of paragraph 12 of Rule XXVI of the Standing Rules of the Senate (relating to the showing of changes in existing law by the provisions of S. 1, as reported by the committee).

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